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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, AS RECEIVER OF DUQUESNE GAS CORPORATION, PETITIONER,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED APRIL 18, 1935.

CERTIORARI GRANTED MAY 13, 1935.

SUPREME COURT OF THE UNITED STATES

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[fol. 1]

IN UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation, Complainant-Appellee-Appellant,

against

MAXIME H. FURLAUD and KINGSTON CORPORATION, Defendants-Appellants-Appellees,

and

BYRON CORPORATION and CHAUCER CORPORATION, Defendants-Appellees,

and

CARLOS REUTER, Defendant

(Cross Appeals)

STATEMENT UNDER RULE XIII.

This action was commenced by the service of a subpœna and bill of complaint on all of the above-named defendants with the exception of the defendant Carlos Reuter on March 24th, 1932.

Carlos Reuter was not served nor did he appear in the above action.

An amended bill of complaint was served and filed on or about the 3rd day of May, 1932.

[fol. 2] The defendants herein moved under equity Rule 20 to compel the complainant to make a further and better statement of the nature of the claim set forth in the amended bill of complaint.

An order was entered on or about the 23rd day of June, 1932 denying the application made on behalf of the defendants under equity Rule 20. The said order was signed by the Hon. Francis G. Caffey, one of the Justices of the United States District Court for the Southern District of New York.

On or about the 5th day of June, 1932, the above-named defendants except Reuter filed their respective answers to the amended bill of complaint herein.

The complainant is George W. McCandless, as Receiver of the Duquesne Gas Corporation.

Ehrich, Royall, Wheeler & Walter are the solicitors for the complainant.

The defendants are Maxime H. Furlaud, Kingston Corporation, Byron Corporation, Chaucer Corporation.

Eppstein & Hirshfield are the solicitors for the said defendants.

There has been no change of parties or attorneys since the commencement of this action.

The trial commenced before the Hon. John C. Knox, District Court Judge sitting in the United States District Court for the Southern District of New York on the 9th day of November, 1932.

A decree was made on the 11th day of May, 1933 and entered on the 12th day of May, 1933 in the sum of $1,834,640.08 together with costs and disbursements, in favor of the complainant and against the defendants, Maxime H. [fol. 3] Furlaud and Kingston Corporation and dismissing the bill of complaint as to the defendants Byron Corporation and Chaucer Corporation on the merits without costs.

The notice of appeal of the defendants, Kingston Corporation and Maxime H. Furlaud, together with assignment of errors, bond for costs and the citation were filed on the 19th day of July, 1933 and the appeal was allowed on the said day.

The bond for costs was approved on the 20th day of July, 1933.

The notice of appeal of the complainant, together with assignment of errors, bond for costs and the citation were filed on the 9th day of August, 1933, and the appeal was allowed on the 10th day of August, 1933.

The bond for costs was approved on the 10th day of August, 1933.

[fol. 4] IN UNITED STATES DISTRICT COURT

SUBPŒNA

E66—185

The President of the United States of America, to Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation, Greeting:

You are hereby commanded to appear before the Judges of the District Court of the United States of America for the Southern District of New York, in the Second Circuit, to answer a bill of complaint exhibited against you in the said Court in Equity, by George W. McCandless, as receiver of Duquesne Gas Corporation and to further do and receive what the said Court shall have considered in this behalf. And this you are not to omit under the penalty on you and each of you of Two Hundred and fifty Dollars ($250).

Witness, Honorable John C. Knox, Judge of the District Court of the United States for the Southern District of New York, on the 23 day of March in the year One Thousand Nine Hundred and Thirty-two and of the Independence of the United States the One Hundred and Fifty-sixth.

(Signed) Charles Weiser, Clerk.

Ehrich, Royall, Wheeler & Walter, Sol'rs.

The defendants are required to file their answers or other defense in the above cause in the Clerk's office on or before the twentieth day after service hereof excluding the day of said service, otherwise the bill aforesaid may be taken pro confesso.

(Signed) Charles Weiser, Clerk. (Seal.)

[fol. 5] In United States District Court, Southern District of New York

In Equity. No. 66-185

George W. McCandless, as Receiver of Duquesne Gas Corporation, Complainant,

against

Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation, Defendants.

Amended Bill of Complaint

To the Honorable the Judge of the District Court of the United States for the Southern District of New York:

The complainant, as Receiver of Duquesne Gas Corporation, brings this, his amended bill of complaint, and alleges:

First: That this is a suit of a civil nature wherein the amount in controversy exclusive of interests and costs is in excess of the sum of $3,000.

Second: That the complainant is a resident of the City of Pittsburgh, and a resident and citizen of the Commonwealth of Pennsylvania; that Duquesne Gas Corporation is a corporation organized and existing under the laws of the Commonwealth of Pennsylvania having its principal office in the City of Washington, Commonwealth of Penn-[fol. 6] sylvania, which lies within the territorial limits of the United States District Court for the Western District of Pennsylvania.

Third: Upon information and belief that defendants Maxime H. Furlaud and Carlos Reuter are residents of the County of New York and of the Southern District of New York; that defendant Kingston Corporation is a corporation organized under the laws of the State of New Jersey; that defendant Byron Corporation is a corporation organized under the laws of the State of Delaware; and that defendant Chaucer Corporation is a corporation organized under the laws of the State of Delaware.

Fourth: That by an order duly made in the United States District Court, in and for the Western District of Pennsyl-

vania, upon the 19th day of January, 1932, in a suit in equity, entitled "Frank T. Harrington, Plaintiff, against Duquesne Gas Corporation, Defendant", in Equity No. 2554, which suit was consolidated with a suit entitled "Central Hanover Bank and Trust Company, as Trustee under First Mortgage of Duquesne Gas Corporation, dated as of March 15, 1930, Plaintiff against Duquesne Gas Corporation, Defendant", In Equity No. 2577, the complainant herein was appointed Receiver of all the assets and property, including choses in action of said Duquesne Gas Corporation, and the complainant has duly qualified and is now acting as such Receiver; that upon petition of the complainant as such Receiver duly filed in the United States District Court, in and for the Southern District of New York, an order was duly made on the 23rd day of March, [fol. 7] 1932, by said last mentioned Court appointing said complainant, George W. McCandless, as Ancillary Receiver of Duquesne Gas Corporation, which last mentioned order duly authorized the complainant, as such Receiver, to bring this suit, and the complainant has duly qualified and is now acting as such Ancillary Receiver.

Fifth: Upon information and belief that on or about the 18th day of July, 1928, a corporation was organized under the laws of the State of New York named Furlaud & Company, Inc. the name of which was later changed to Furlaud, Reuter & Company, Incorporated and later changed to Winchelsea Holding Corporation, and a certificate of dissolution of which was filed on the 27th day of October, 1931; that defendants Maxime H. Furlaud, Carlos Reuter and/or their mere nominees or dummies were at all times the only stockholders of said corporation in this paragraph mentioned, and that they and/or their mere nominees or dummies were at all times the directors of said corporation, and that at the time of the filing as aforesaid of the certificate of dissolution of said corporation, said defendants Furlaud, Reuter and/or their mere nominees or dummies were all of the directors and stockholders of the corporation in this paragraph mentioned.

Sixth: Upon information and belief that the certificate of incorporation of said Duquesne Gas Corpartion was filed in the office of the Secretary of the Commonwealth of Pennsylvania on the 13th day of February, 1930, and since

the completion of its organization shortly after that date has owned and operated natural gas wells, pipe lines and other property incidental thereto, all situated in the West-
[fol. 8] ern District of the State of Pennsylvania; the organization of said Duquesne Gas Corporation was brought about by the defendants Maxime H. Furlaud and Carlos Reuter, and they acted as and were the promoters of such corporation. One Randolph C. Coleman, one McLane Tilton and one Frank A. Cabeen, Jr. were the original directors named in the certificate of incorporation and acted as such directors until the 7th day of April, 1930; said Coleman, Tilton and Cabeen were the mere nominees of defendants Furlaud and Reuter, and in all the acts which they performed as directors of said Duquesne Gas Corporation they acted merely at the behest of and under the instructions of said Furlaud and said Reuter. One Otto E. Schuller, one Thomas W. D. Duke, one Henry T. Wynn and one Charles C. Henderson, together with the defendants Furlaud and Reuter became directors of said Duquesne Gas Corporation on the 7th day of April, 1930, on which date said Coleman, Tilton and Cabeen resigned and ceased to act as directors. Said Schuller was an employee of defendants Furlaud and Reuter or of said corporation, sometimes known as Furlaud & Company, Inc. Said Duke was employed as an attorney at law by the defendants Furlaud and Reuter to draw the papers in carrying out the various proceedings herein alleged. They, as well as the said Wynn and Henderson, were the mere nominees of the defendants Furlaud and Reuter in acting as such directors and in all the steps taken by them as such directors they acted under the instructions and at the behest of said defendants Furlaud and Reuter.

Seventh: Upon information and belief that during or about the months of March and April 1930, defendants Fur-
[fol. 9] laud and Reuter caused such steps to be taken by said Duquesne Gas Corporation as to bring about the authorization of a first mortgage of $4,000,000 securing an issue of $4,000,000 of first mortgage bonds of Duquesne Gas Corporation, an indenture covering the issue of $1,000,000 of so-called Convertible 6½% Secured Gold Notes and the issuance of 675,000 shares of no par value common stock.

Eighth: Upon information and belief that during or about the months of March and April 1930, the defendants

Furlaud and Reuter acting through the above described corporation, then known as Furlaud & Company, Inc., made, as the banking house of issue, a public offering of the $4,000,000 of said bonds at the offering price of 97½ and a public offering of the $1,000,000 of the said notes at 98, and through such banking house of said Furlaud & Company, Inc. stated in a bond circular publicly issued and advertised by them that, in the case of said bonds "These bonds were issued by the corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes", and in the case of said notes that "These notes are issued by the corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes"; that as a result of the steps so taken by the defendants Furlaud and Reuter at the time aforesaid, or shortly thereafter, the whole amount of said $4,000,000 of said bonds and of said $1,000,000 of said notes were issued and distributed to the public at said prices or at prices approximating the same, or at an aggregate purchase price for said bonds of approximately $3,900,000 and [fol. 10] of said notes of $980,000, or at an aggregate sales price for both said bonds and notes of approximately $4,880,000.

Ninth: Upon information and belief that at the time of the issuance, sale and distribution of said bonds and notes by the defendants Furlaud and Reuter, as aforesaid, said last mentioned defendants had made arrangements for the acquisition for said Duquesne Gas Corporation of various natural gas wells and properties situated in Southwestern Pennsylvania; that the aggregate price of said properties so arranged to be acquired for Duquesne Gas Corporation was $2,572,989; that during or about the month of April 1930, said gas properties were conveyed by the various owners thereof to said Duquesne Gas Corporation in consideration of the payment by Duquesne Gas Corporation of sums of money as the various purchase prices thereof aggregating the said sum of $2,572,989; that said sum of $2,572,989 was paid out of the proceeds of the sale of said bonds and notes.

Tenth: Upon information and belief that except for the payment as aforesaid for the benefit of said Duquesne Gas Corporation of the said sum of $2,572,989 and except also

for the payment into the treasury of said Duquesne Gas Corporation out of the proceeds of the sale of said bonds and notes of the sum of $365,000, and except for the payment out of the proceeds of the sale of such bonds and notes of such amount as may be considered a legitimate bankers' commission for the distribution and sale of said bonds and notes, and as may be considered proper organization expenses for the organization of Duquesne Gas Corporation, [fol. 11] said Duquesne Gas Corporation received nothing either directly or indirectly out of the approximately $4,880,000, which was the proceeds of the sale of said bonds and notes.

Eleventh: That the defendants Furlaud and Reuter caused all of the proceeds of the sale of said bonds and notes beyond the amount of said sum of $2,572,989 plus said sum of $365,000 (other than the legitimate bankers' commissions for the sale of said bonds and notes and legitimate expenses of organization of said corporation) to be diverted from the Duquesne Gas Corporation for whose use and benefit the proceeds of the sale of said bonds and notes was intended and defendants Furlaud and Reuter fraudulently misappropriated said moneys to their own use.

Twelfth: That defendants Furlaud and Reuter caused said Duquesne Gas Corporation to issue to them or to their nominees or dummies, including the defendants Kingston Corporation, Byron Corporation and Chaucer Corporation, 675,000 shares of the capital stock of said Duquesne Gas Corporation and sold 85,000 shares thereof in the name of defendants Byron Corporation and Chaucer Corporation for the sum of $850,000 cash, which sum of $850,000 was retained by the defendants Furlaud and Reuter and converted to their own uses through the agency of said last two mentioned defendant corporations.

Thirteenth: Upon information and belief that said Duquesne Gas Corporation has received out of the proceeds of the sale of said bonds and said notes, as well as out of the sale of said 85,000 shares of stock, or in consideration for the issuance of the balance of said 675,000 shares of stock, [fol. 12] nothing whatsoever except that, as aforesaid, it received the title to the gas properties purchased for it by defendants Furlaud and Reuter at a cost of $2,575,989 and $365,000 of working capital and whatever benefits arose

from the organization of the corporation and from the services of the defendants in selling its securities.

Fourteenth: Upon information and belief that defendants Furlaud and Reuter were the promoters of said Duquesne Gas Corporation; that they caused it to be organized; that all the steps which were taken for the consummation of its incorporation, organization, issuance of its said bonds, notes and stocks were taken under the direction and at the behest of defendants Furlaud and Reuter; that they stand in a fiduciary relation to said Dequesne Gas Corporation; that defendants Furlaud and Reuter are accountable to the corporation for the proceeds derived from the issuance and sale by them as aforesaid of all of said securities of said corporation.

Fifteenth: Upon information and belief that the moneys diverted by defendants Furlaud and Reuter from the proper uses of said Duquesne Gas Corporation and misappropriated by defendants Furlaud and Reuter (even after the allowance of a fair and proper banking commission for the sale of said securities and after a fair and proper allowance for the expenses of the organization of Duquesne Gas Corporation) is not less than $2,500,000.

Sixteenth: Upon information and belief that the follow-
[fol. 13] ing were some of the additional steps taken by defendants Furlaud and Reuter in connection with the organization of said Duquesne Gas Corporation, the acquisition of its said gas properties and the issuance of its said securities and the diversion and misappropriation of its funds:

Defendants Furlaud and Reuter caused to be organized under the laws of the State of New Jersey the defendant Kingston Corporation, of which corporation they or their mere nominees or dummies were the only stockholders and of which they or their mere nominees or dummies were the only directors and officers; that defendants Furlaud and Reuter also caused to be organized under the laws of the State of Delaware the defendant Byron Corporation, that the stockholders of said Byron Corporation were defendants Furlaud and Reuter or mere nominees and dummies of Furlaud and Reuter, and the directors and officers of said Byron Corporation were mere nominees or dummies of said Furlaud and Reuter; that defendants Furlaud and

Reuter also caused to be organized under the laws of the State of Delaware the defendant Chaucer Corporation, that the stockholders of said Chaucer Corporation were defendants Furlaud and Reuter or mere nominees and dummies of Furlaud and Reuter, and the directors and officers of said Chaucer Corporation were mere nominees or dummies of said Furlaud and Reuter; that option agreements for the purchase of the various gas properties which were acquired as aforesaid for said Duquesne Gas Corporation were taken in the name of defendant Kingston Corporation, the sum total of which option prices was $2,572,989; that defendants Furlaud and Reuter also caused a contract to be [fol. 14] made between said corporation, sometimes known as Furlaud & Company, Inc., and Duquesne Gas Corporation for the sale by Duquesne Gas Corporation to said Furlaud & Company, Inc. of $2,700,000 of said bonds and $1,000,000 of said notes, the contract price being 90 for said bonds and 88 for said notes, or an aggregate contract price of $3,310,000; that before the issuance and delivery of said bonds and notes which were sold as aforesaid, defendants Furlaud and Reuter arranged with the sellers of the several properties (the optioners) that such sellers or optioners should deposit in escrow in various banks situated in several towns in Western Pennsylvania convenient to the optioners, title papers conveying direct to Duquesne Gas Corporation said several gas properties under escrow agreements providing that upon drafts upon the Duquesne Gas Corporation for the respective purchase prices being taken up and paid, said title papers should be definitely delivered; that the date for definitive deliveries and the payment of the respective purchase prices was adjourned from time to time to correspond with the date for the delivery to various investment houses under the bankers syndicate for the sale of said bonds and notes and the receipt of the purchase price of said securities; that on the 7th day of April, 1930, delivery was made of a large part of said bonds and all of said notes and on that day drafts were taken up and paid out of the proceeds of the sale of said bonds and notes for the purchase price of said several gas properties; that the amount of the purchase price of said several gas properties was said sum of $2,572,989; that under date of April 7, 1930, a written paper called "Agreement of Reorganization between Duquesne Gas Corpora-

[fol. 15] tion and Kingston Corporation of New Jersey" was signed, which bears the signatures of "Kingston Corporation by M. A. Furlaud, President, attested Robert Halporn, Assistant Secretary" and of Duquesne Gas Corporation by Walter G. Krog, Vice-President, by Robert Halporn, Assistant Secretary"; that said Krog and Halporn were both employees of defendants Furlaud and Reuter or of said corporation hereinabove described, sometimes known as Furlaud & Company, Inc.; that under said so-called agreement of reorganization for an alleged consideration of the transfer by defendant Kingston Corporation to said Duquesne Gas Corporation of said gas properties, said Duquesne Gas Corpporation agreed to pay $3,015,000 stated to be the amount which defendant Kingston Corporation would be obligated to pay at the Central Hanover Bank and Trust Company and by which said Duquesne Gas Corporation also agreed to issue and deliver to said Kingston Corporation 535,000 shares of its common stock and $1,300,000 in principal amount of its 6% Mortgage Convertible Gold Bonds; that soon thereafter defendant Kingston Corporation went through the form of granting options to various employees or dummy corporations of defendants Furlaud and Reuter or of said corporation, sometimes called Furlaud & Company, Inc., for the purchase at 50c a share of 510,000 shares of said capital stock of said Duquesne Gas Corporation, which so-called options were then caused by defendants Furlaud and Reuter to be assigned to the extent of 225,000 shares each to defendants Byron Corporation and Chaucer Corporation; immediately or soon after the 7th day of April, 1930, defendants Furlaud and Reuter caused defendant Kingston Corporation to go through the [fol. 16] form of declaring a dividend in kind to its stockholders of said $1,300,000 in face amount of bonds of Duquesne Gas Corporation and 25,000 shares of the capital stock of Duquesne Gas Corporation; that defendants Furlaud and Reuter caused the original 1,000 shares of the capital stock of said Duquesne Gas Corporation to be subscribed for by three individuals who are mere nominees or dummies of defendants Furlaud and Reuter, which subscriptions were assigned to said corporation sometimes known as Furlaud & Comapny, Inc., and defendants Furlaud and Reuter caused a subscription for 139,000 additional shares to be made by said Furlaud & Company, Inc.,

and accepted by Duquesne Gas Corporation at 50c a share, or a total of 140,000 shares; that thereafter defendants Furlaud and Reuter acting through defendants Byron Corporation and Chaucer Corporation sold 85,000 of said last mentioned shares at $10 a share to one J. J. Bergen for the total sum of $850,000 in cash and as an incident thereto caused said shares of stock to be listed on the New York Curb market; that the purchase price of $850,000 for said 85,000 shares of stock was received to the extent of $425,000 thereof by defendant Byron Corporation and to the extent of $425,000 thereof by defendant Chaucer Corporation; that thereafter defendants Furlaud and Reuter organized what is known as the Secondary Syndicate for the sale of $1,300,000 in face amount of the bonds of Duquesne Gas Corporation which were received by them as above stated through the mechanism of said Kingston Corporation; that said additional bonds were to be sold by the distributing group of security dealers organized by the defendants to public investors at the price then (August 1930) [fol. 17] prevailing on the New York Curb for such bonds which was about 86; that all of said additional $1,300,000 of bonds were sold at about that time and about that price less a commission to dealers varying from two to four points according to the amount of bonds placed by such dealers and that defendants Furlaud and Reuter either directly or through said corporation, sometimes known as Furland & Company, Inc. received from the proceeds of the sale thereof the sum of approximately $1,100,000.

Seventeenth: That the complainant, as Receiver, is entitled on behalf of Duquesne Gas Corporation to have the defendants account to the corporation for the funds or moneys coming into their hands or into the hands of any of them or their agents or representatives from the sale of the securities of said Duquesne Gas Corporation or of any of said securities, and for the disposition made of such funds or moneys and to make restitution for any or all of such funds or moneys wrongfully diverted from Duquesne Gas Corporation and misappropriated or converted by the defendants or any of them to their own uses and for any or all secret or excessive profits taken or retained by them or any of them; that your complainant has no adequate remedy at law and your complainant's rights may only be properly adjudicated in this Court of Equity.

Wherefore, your complainant prays as follows:

I. That the defendants Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation, and each of them, be compelled and required to account to said Duquesne Gas Corporation and [fol. 18] to complainant as Receiver of said Duquesne Gas Corporation for all funds or moneys coming into the hands of them or any of them or of the agents or representatives of any of them or in the hands of any one else acting with or for them from the sale of the bonds, notes and shares of stock of said Duquesne Gas Corporation.

II. That the Court shall decree the payment by the defendants and each of them to the complainant as Receiver of Duquesne Gas Corporation of such sum or sums of money as said Duquesne Gas Corporation or your complainant as its Receiver shall appear upon such account to be entitled.

III. The complainant prays for such other and further relief as to the Court appears to be just.

IV. That process of subpœna issue herein in due course directed to the defendants herein and each of them.

Ehrich, Royall, Wheeler & Walter, Solicitors for the Complainant, Office & P. O. Address, 20 Exchange Place, Borough of Manhattan, New York City. Ralph Royall and Clark Miller and William A. Magee, of Pittsburgh, of Counsel.

(Verified on April 27, 1932, by George W. McCandless.)

[fol. 19] In United States District Court, Southern District of New York

[Title omitted]

Order to Show Cause—Kingston Corporation

Upon the annexed affidavit of Ira W. Hirshfield verified the 19th day of May, 1932, and upon the amended bill of complaint annexed hereto, and upon all the proceedings heretofore had herein,

Now on motion of Eppstein & Hirshfield, solicitors for the defendant, Kingston Corporation, it is

Ordered that George W. McCandless, as Receiver of Duquesne Gas Corporation, the complainant herein, show cause before one of the Judges of the United States District Court in and for the Southern District of New York at a term thereof for the hearing of motions to be held in the old Post Office Building in the Borough of Manhattan, City of New York, Room 235, on the 24th day of May, 1932, at 10:30 o'clock in the forenoon of that day or as soon thereafter as counsel can be heard why an order should not be [fol. 20] made herein requiring the complainant (1) to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint by separately stating and numbering the causes of action attempted to be set forth therein; (2) to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint herein by stating definitely and specifically the ultimate facts showing how it is claimed that the defendants Furlaud and Reuter caused the proceeds of the sale of the bonds and notes of the Duquesne Gas Corporation beyond the amount of $2,572,989.00 plus $365,000.00 (other than the legitimate bankers' commissions for the sale of said bonds and notes and legitimate expenses of organization of said corporation) to be diverted from the Duquesne Gas Corporation as alleged in paragraph "Eleventh" of the amended bill of complaint; (3) to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint herein by stating definitely and specifically the ultimate facts upon which it is claied that the defendants Furlaud and Reuter caused the proceeds of the sale of the bonds and notes of the Duquesne Gas Corporation, beyond the amount of $2,572,989. plus $365,000. (other than the legitimate bankers' commissions for the sale of said bonds and notes and legitimate expenses of organization of said corporation) to be fraudulently misappropriated as alleged in paragraph "Eleventh" of the amended bill of complaint; and (4) to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint herein by stating definitely and specifically [fol. 21] how it is claimed that the defendants Furlaud and Reuter misappropriated and diverted moneys from the

proper uses of the said Duquesne Gas Corporation as alleged in paragraph "Fifteenth" of the amended complaint; and it is further

Ordered that, sufficient cause appearing therefor, the time of the defendant Kingston Corporation to answer the amended complaint herein be and the same hereby is extended until ten days after the determination of this motion and the service of an order with notice of entry thereof upon the solicitors for the defendant, in the event that the motion is decided adversely to the defendant, with leave to said defendant on the hearing of this motion to apply for a further extension; and it is further

Ordered that service of a copy of this order to show cause and a copy of the affidavit hereto annexed upon the solicitors for the complainant on or before the 20th day of May, 1932, shall be deemed good and sufficient service.

Dated, New York, May 19th, 1932.

Francis G. Caffey, U. S. D. J.

[fol. 22] In United States District Court, Southern District of New York

[Title omitted]

Affidavit of Ira W. Hirshfield in Support of Order to Show Cause on Behalf of Kingston Corporation

State of New York,
County of New York, ss:

Ira W. Hirshfield, being duly sworn, deposes and says:

I am an attorney and counsellor at law of the State of New York and have been admitted to practice in the United States District Court for the Southern District of New York.

I am a member of the firm of Eppstein & Hirshfield, the solicitors for the above named defendants, with the exception of the defendant Carlos Reuter, who has not been served and who has not appeared.

I am familiar with all of the facts in the above entitled action.

This affidavit is made by me in support of an application on behalf of the defendant Kingston Corporation, pursuant

[fol. 23] to Rule 20 of the Equity Rules, for an order requiring the complainant herein to make a further and better statement of the nature of the claims contained in the amended complaint herein for the reasons hereinafter set forth.

On the 7th day of April, 1932, the defendants Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation were served with subpœnas in the above matter. Subsequently, answers were interposed by the defendants, Furlaud and the Kingston Corporation, and an order to show cause was granted requiring the complainant to show cause why the action should not be dismissed in so far as Byron Corporation and Chaucer Corporation were concerned upon the ground that the said corporations were not doing business within the Southern District of New York.

Subsequently, the aforesaid motions were withdrawn and a stipulation was entered into extending the time of the said Byron Corporation and Chaucer Corporation to answer until the 30th day of April, 1932.

By an order to show cause dated the 26th day of April, 1932, and served upon the solicitors for the defendants above named on the 27th day of April, 1932, the complainant moved this Court for permission to serve an amended complaint. This application was granted upon consent of all parties and upon condition that the defendants be permitted to serve answers to the amended complaint or to make any motions with respect thereto within 20 days from the date of the service upon the solicitors for the defendant of the said amended complaint.

An amended complaint was served upon the solicitors for [fol. 24] the defendants on the 30th day of April, 1932, a copy of which is annexed hereto and made a part hereof as if set forth in full.

The amended complaint alleges that by an order of this Court, made on the 23rd day of March, 1932, the complainant was appointed ancillary receiver of the Duquesne Gas Corporation. The said order authorizes the complainant "to bring an action against the promoters of said corporation, including Maxime H. Furlaud and Carlos Reuter, for an accounting and for the restitution of funds fraudulently diverted and misappropriated and for secret and excessive profits".

It will thus be seen from the quoted portion of the order appointing the complainant ancillary receiver of the Duquesne Gas Corporation, that the receiver has been authorized to maintain two actions against the defendants herein:

(1) An action for the restitution of funds fraudulently diverted and misappropriated and (2) an action to recover secret and excessive profits.

This motion has been brought on to compel the complainant to make a further and better statement of the nature of the claim asserted in his amended complaint for the following reasons:

1. That the complainant has joined together in one cause of action two separate and distinct causes of action without any attempt on the part of the complainant to separately state and number them. This has resulted in the amended complaint being of such a character as to confuse the real issues involved and to make it impossible for the defendant to separate those allegations which relate to the claim for [fol. 25] the restitution of funds fraudulently diverted and misappropriated from the facts alleged with reference to the claim for secret and excessive profits.

2. That it appears from the amended complaint that the complainant has not complied with Rule 25 of the Equity Rules in that he has failed to make a short and simple statement of the ultimate facts upon which the complainant seeks relief. The complainant has pleaded conclusions of law rather than statements of ultimate facts insofar as he seeks to recover for misappropriation of funds belonging to the Duquesne Gas Corporation.

In order to more clearly understand the basis of the defendant's objection herein, an examination of the essential allegations of the amended complaint is requisite.

In Paragraph "Seventh" of the amended complaint, the complainant alleges that the defendants Furlaud and Reuter caused the Duquesne Gas Corporation to issue (1) a first mortgage of $4,000,000 to secure an issue of a like amount of first mortgage bonds, (2) an indenture covering the issue of $1,000,000 of convertible gold notes, and (3) 675,000 shares of common stock.

It is claimed that the defendants Furlaud and Reuter, acting through a corporation known as Furlaud & Company, Inc., made a public offering of the bonds and the notes and realized from the sale thereof $4,880,000. It is claimed that representations were made in the bond and note circulars that the securities in question were issued for various corporate purposes.

It is then asserted that out of the monies derived from the sale of these securities $2,572,989 was spent in acquiring, for the Duquesne Gas Corporation, various natural gas [fol. 26] wells and properties situated in Southwestern Pennsylvania and, in addition, $365,000 was paid into the treasury of the Duquesne Gas Corporation for working capital. The balance, less a legitimate bankers' commission and expenses of the organization of the Duquesne Gas Corporation, it is claimed, was fraudulently misappropriated by the defendants Furlaud and Reuter to their own uses.

It is then asserted that the individual defendants Furlaud and Reuter caused the Duquesne Gas Corporation to issue to them or their nominees 675,000 shares of the Common Stock of Duquesne Gas Corporation and that they subsequently sold 85,000 shares of this stock in the name of Byron Corporation and Chaucer Corporation for the sum of $850,000 which sum was retained by the defendants Furlaud and Reuter for their own use, through the agency of Byron and Chaucer Corporations.

The complainant then makes general allegations that the defendants Furlaud and Reuter misappropriated and diverted the funds belonging to the Duquesne Gas Corporation to the extent of at least $2,500,000.

Deponent respectfully contends that the allegations made by the complainant that the defendants Furlaud and Reuter and their so-called instrumentalities Furlaud & Company, Inc., Kingston Corporation, Byron and Chaucer Corporations, converted and misappropriated to their own uses funds of the Duquesne Gas Corporation, are not statements of ultimate facts as required by Rule 25 of the Equity Rules but are merely conclusions of law which do not properly apprise the defendants of the claim which the complainant is attempting to assert against them.

[fol. 27] From the allegations appearing in the amended complaint, the defendant does not know whether the com-

plainant is accusing the defendants of direct theft of the funds in question or whether the complainant has some other type of fraudulent and guilty conduct in mind. In fact, the amended complaint makes confusion more confounded when we examine paragraph "Sixteenth" wherein it is alleged that "the following were some of the additional steps taken by the defendants, Furlaud and Reuter, in connection with the organization of the said Duquesne Gas Corporation, the acquisition of its said gas properties and the issuance of its said securities and the diversion and misappropriation of its funds."

In paragraph "Sixteenth", there is not a single allegation that reveals any fraud on the corporation or any misappropriation of funds. The only question presented is one of promoters' profits. It is impossible for the defendant to know from the amended complaint whether the complainant intends on the trial to charge a fraudulent diversion of funds or merely a situation of promoters' profits. This state of affairs requires a better statement by the complainant of its claim and a statement of ultimate facts rather than conclusions of law as required under Rule 25 of the Equity Rules.

The complainant in paragraph "Sixteenth" apparently has attempted to show that through the instrumentality of various corporations the individual defendants, Furlaud and Reuter, succeeded in obtaining for themselves very large promoters' profits. He has set forth in detail the various steps claimed to have been taken by the individual defendants and their so-called controlled corporations to [fol. 28] enable the individual defendants to realize this alleged profit. These allegations tend to charge that all of the profits claimed to have been realized were derived from the sale of securities of the Duquesne Gas Corporation acquired by Furlaud and Reuter and their so-called nominees. No suggestion is made in that paragraph which intimates that the defendants had been guilty of any fraudulent practices whatsoever or that they had misappropriated or diverted funds of the corporation.

Any attempt by the defendant to answer the amended complaint herein is difficult. The complainant has alleged misappropriations and diversions. There are allegations in paragraph "Sixteenth" of the amended complaint which attempt to set forth all of the steps by which all of the

bonds, notes and stock of the Duquesne Gas Corporation were acquired. We cannot determine from this paragraph whether these are the alleged ultimate facts upon which complainant relies to show fraudulent diversion and misappropriation of funds or whether they are relied on solely to show promoters' profits. It, therefore, becomes very essential for the complainant to make a better statement of his case and to properly apprise the defendant as to just what the diversions and/or misappropriation consist of.

The defendant contemplates bringing on a motion to dismiss the amended bill herein on the ground that it does not state facts sufficient to constitute a cause of action against the defendant, but hesitates to do so unless the complainant is required to make a further and better statement of his case because some of the general (and improperly pleaded) allegations might prevent the granting of such an application.

In the case of Rogers v. Hill, 53 Fed. (2nd) 395, decided [fol. 29] by Mr. Justice Woolsey, one of the District Judges for the Southern District of New York, the Court in granting a motion similar to this one stated at page 398:

"The purpose of this motion (made under Equity Rule 20) is to get the plaintiff so to allege his cause of action as to enable a motion for judgment on the pleadings to be made by the defendants, and thus to test the validity, as a matter of law, of the by-law of February 21, 1912 above referred to."

Your deponent therefore respectfully prays that an order be entered herein requiring the complainant:

1. To make a further and better statement of the nature of the claim and/or claims set forth in the amended complaint by separately stating and numbering the causes of action attempted to be set forth therein.

2. To make a further and better statement of the nature of the claim and/or claims set forth in the amended complaint herein by stating definitely and specifically the ultimate facts showing how it is claimed that the defendants Farland and Reuter caused the proceeds of the sale of the bonds and notes of the Duquesne Gas Corporation beyond the amount of $2,572,989 plus $365,000 (other than the legitimate bankers' commissions for the sale of said bonds

and notes and legitimate expenses of organizaation of said corporation) to be diverted from the Duquesne Gas Corporation as alleged in paragraph "Eleventh" of the amended bill of complaint.

[fol. 30] 3. To make a further and better statement of the nature of the claim and/or claims set forth in the bill herein by stating definitely and specifically the ultimate facts showing how it is claimed that the defendants Furlaud and Reuter caused the proceeds of the sale of the bonds and notes of the Duquesne Gas Corporation, beyond the amount of $2,572,989 plus $365,000 (other than the legitimate bankers' commissions for the sale of said bonds and notes and legitimate expenses of organization of said corporation) to be fraudulently misappropriated as alleged in paragraph "Eleventh" of the amended bill of complaint.

4. To make a further and better statement of the nature of the claim and/or claims set forth in the bill herein by stating definitely and specifically the ultimate facts upon which it is claimed that the defendants Furlaud and Reuter misappropriated and diverted moneys from the proper uses of the said Duquesne Gas Corporation.

The reason why this application is made by order to show cause rather than by the usual notice of motion is that the 20th day of May, 1932, is the last day for the defendant to interpose an answer to the amended bill of complaint herein or to move with respect thereto.

This period will expire before the first possible return date of a motion made in the ordinary course by notice of motion and before the decision of this motion. It is therefore essential that the defendant's time to answer be extended until an opportunity is had for the Court to determine this motion.

Wherefore your deponent respectfully prays that an order be entered herein compelling the complainant to make a [fol. 31] further and better statement of the nature of the claim and/or claims alleged in the amended complaint, as set forth herein; that the defendant's time to answer the complaint herein be extended until twenty days after the determination of this motion and the service of an order with notice of entry thereof upon the solicitors for the defendant, in the event that the motion is determined adversely to the defendant herein, and for such other and

further relief as to the Court may seem just and proper, for all of which no previous application has been made.

Ira W. Hirshfield.

Sworn to before me, this 19th day of May, 1932.

Marion Goodman, Notary Public.

[fol. 32] In United States District Court, Southern District of New York

[Title omitted]

Statement as to Orders to Show Cause of Other Defendants

Orders to show cause were obtained on behalf of the defendants, Maxime H. Furlaud, Byron Corporation and Chaucer Corporation, all dated May 19th, 1932 and signed by the Hon. Francis G. Caffey, one of the Justices of the United States District Court for the Southern District of New York.

The said orders to show cause are similar in all respects to the order to show cause obtained on behalf of the defendant Kingston Corporation, with the exception of changes in pronouns and adjectives required in each particular case.

[fol. 33] In United States District Court, Southern District of New York

[Title omitted]

Statement as to Affidavits of Ira W. Hirshfield as to Orders to Show Cause on Behalf of Other Defendants

Separate affidavits of Ira W. Hirshfield, all sworn to on the 19th day of May, 1932, were submitted in support of the orders to show cause obtained on behalf of the defendants, Maxime H. Furlaud, Byron Corporation, and Chaucer Corporation, respectively.

These affidavits are similar in all respects to the affidavit of Ira W. Hirshfield, sworn to on the 19th day of May, 1932 and submitted in support of the order to show cause ob-

tained on behalf of the defendant, Kingston Corporation, with the exception of such changes in pronouns and adjectives as might have been required in each particular case.

[fol. 34] IN UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK

[Title omitted]

AFFIDAVIT OF RALPH ROYALL IN OPPOSITION TO MOTION MADE BY DEFENDANTS

STATE OF NEW YORK,
County of New York, ss.:

Ralph Royall, being duly sworn, deposes and says that he is a member of the firm of Ehrich, Royall, Wheeler & Walter, solicitors for the complainant-receiver in the above entitled suit, and is thoroughly familiar with the proceedings heretofore had herein.

This affidavit is made in opposition to the separate motions made by the defendants' Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, for an order under Equity Rule No. 20 requiring the complainant to make a further and better statement of the nature of the complainant's claim.

The original bill of complaint was served herein upon all the defendants excepting the defendant Reuter on the 24th day of March, 1932. On the 12th day of April, 1932, the defendants Byron Corporation and Chaucer Corporation appearing specially by Messrs. Eppstein & Hirshfield as [fol. 35] their solicitors obtained an order requiring the complainant to show cause why an order should not be made quashing the service of the subpoena upon the defendants Chaucer Corporation and Byron Corporation. This motion was argued on the 15th day of April before Judge Coleman who upon that date made an order appointing a Referee to take testimony as to whether or not these two corporations were doing business within the Southern District of New York so as to be amenable to process. Upon the Referee's summons and subpoena duces tecum being served upon one Paul M. Coonrod to appear before the Referee and produce the books of these corporations, their

solicitors filed a general appearance herein on their behalf and thus dispensed with the necessity of appearing before the Referee. Said Coonrod who made the affidavit upon which the motions to quash were based is the Secretary of the defendants Byron Corporation and Chaucer Corporation and is a lawyer in the employ of Messrs. Eppstein & Hirshfield. While the above proceedings were going forward the defendants Maxime H. Furland and Kingston Corporation appeared herein by Messrs. Eppstein & Hirshfield as their solicitors and on the 18th day of April served their answers to the original bill of complaint. The calendar number is 2392.

On being served with the motion papers by the defendants Byron Corporation and Chaucer Corporation upon the motion to quash service upon them, your deponent went to Pittsburgh, Pennsylvania and there obtained the affidavit of one Robert A. McShea, Jr., verified the 16th day of April, 1932, and filed herein on behalf of the complainant in opposition to such motions. Said McShea, who is a certified [fol. 36] public accountant and an accountant of the staff of the Bureau of Statistics of the Public Service Commission of the Commonwealth of Pennsylvania, had been instructed by that Commission to investigate the facts relating to the issuance by the defendants of the securities of Duquesne Gas Corporation, and Mr. McShea set forth in his affidavit certain detailed facts respecting the participation of the defendants Byron Corporation and Chaucer Corporation in the issuance of these securities, and these facts as set forth in such affidavit showed among other things that, to the extent of $850,000 of the moneys received by the defendants out of the securities of Duquesne Gas Corporation sold by them, such moneys had come in the first instance into the hands of the defendants Byron Corporation and Chaucer Corporation. This particular fact had not previously come to the knowledge of the complainant or his solicitors, and a motion was thereupon made upon behalf of the complainant and an order obtained upon the 29th day of April, 1932, permitting the complainant to file and serve the amended bill of complaint herein. The amended bill of complaint was served upon Messrs. Eppstein & Hirshfield upon the 30th day of April, 1932.

Upon the 20th day of May, 1932, the solicitors for the complainant received from Messrs. Eppstein & Hirshfield, the solicitors for the defendants Maxime H. Furland, Kings-

ton Corporation, Byron Corporation and Chaucer Corporation four similar orders to show cause upon similar moving papers for an order requiring complainant to restate his claims under Rule #20 of the Federal Equity Rules and containing an extension of time of all the defendants to answer the amended bill of complaint until ten days after dispositon of the motions.

[fol. 37] The suit is for an accounting and the prayers for relief in the original and amended complaints are identical and the relief asked is that the defendants and each of them be compelled to account to Duquesne Gas Corporation and to complainant as its Receiver for all funds or moneys coming into the hands of them or any of them from the sale of the bonds, notes and shares of stock of Duquesne Gas Corporation.

The amended bill of complaint differs from the original bill of complaint, except for a few slight textual changes, only in that (1) paragraph Twelfth thereof was revised so as specifically to allege that $850,000 of the proceeds of the sale of securities of Duquesne Gas Corporation was in the first instance received by defendants Byron Corporation and Chaucer Corporation; and (2) that paragraph Third was revised so as to allege that the defendants Byron Corporation and Chaucer Corporation were Delaware corporations instead of New York corporations as alleged in the original bill of complaint.

The complaint sets forth in considerable detail the facts surrounding the organization of the defendant Duquesne Gas Corporation and the issuance of its securities; it alleges that the defendants Furlaud and Reuter were the promoters of the corporation; it alleges the various steps that were taken by them in promoting and organizing the corporation and in selling its securities; it alleges that the defendants Kingston Corporation, Chaucer Corporation and Byron Corporation as well as the corporation variously known as Furlaud & Company, Furlaud, Reuter & Company and Winchelsea Holding Corporation (now dissolved) were all of them corporations created by Furlaud and Reuter, of which [fol. 38] they were the owners of all of the capital stock and the officers of all of which were the defendants Furlaud and Reuter or their mere nominees or dummies; it alleges that these various corporations were used by the defendants Furlaud and Reuter in connection with a rather elaborate series of steps in accomplishing the promotion and organi-

zation of the Duquesne Gas Corporation and the sale of its securities and how such corporations were used and what the steps taken were. It is submitted that a reading of the amended bill of complaint will show that, although the proceedings taken by these defendants in diverting and misappropriating the assets of Duquesne Gas Corporation were involved and elaborate, they are clearly set forth in chronological order. It is also submitted that such facts so alleged can bear only the ultimate inference that the defendants stood and stand in a fiduciary relationship to the defendant Duquesne Gas Corporation and that in such relationship they are accountable to the corporation and to its Receiver for all of the moneys coming into their hands or the hands of any of them from the sale of the securities of Duquesne Gas Corporation, and the bill alleges such fiduciary relationship. The bill also sets forth clearly and in detail the amount of the moneys alleged to have come into the hands of the defendants as such fiduciaries and the amount thereof which found its way into the treasury of Duquesne Gas Corporation to which they stood in the fiduciary relationship and the amount wrongfully diverted and misappropriated by the defendants from such corporation which is approximately $2,500,000.

The suit as above stated is a suit for an accounting by persons standing in a fiduciary relationship. The relief flowing from the bill of complaint in a suit such as the [fol. 39] instant one is in the first instance an interlocutory decree for an accounting for which purpose it is requisite to allege and prove only facts and circumstances sufficient to establish the fiduciary relationship and that the fiduciaries have failed to account. The details of the proceedings and steps taken by the fiduciaries in the nature of things await disclosure until the Master is appointed to take the accounts pursuant to the interlocutory decree under Rule 59 when the defendant fiduciaries are required to bring their accounts before the Master under Federal Equity Rule 63 and to set out in detail all the steps and proceedings which they have taken. In this instance the Receiver has been able to obtain considerable detailed information concerning the steps of these defendants as fiduciaries to the corporation in promoting it and organizing it and selling its securities and diverting and misappropriating the proceeds thereof and has thus been able to set out in his bill of complaint such facts and circumstances in consider-

ably more detail than would ordinarily be the case in a suit of this nature.

The motions of the defendants come to this: that in an Equity suit for an accounting the bill of complaint must set forth the details of each and every step of the defaulting fiduciaries. Such a position is directly contrary to the fundamental conceptions underlying a suit of this nature. It is because a person to whom another stands in the relation of fiduciary is presumed not to know or to be able to ascertain the conduct of his fiduciary except as his fiduciary shall account to him that suits for an accounting are in a very separate category in which the procedure has become established that for the purposes of such a suit it is neces- [fol. 40] sary for the complainant to allege and prove only the fiduciary relationship and the failure to account whereupon an interlocutory decree for an accounting is made, requiring the accounting fiduciary to make full disclosure before the Master. They particularize four things: (1) That the separate causes of action should be separately stated and numbered. Manifestly, there is but one cause of action, viz. a cause of action requiring the defendants to account; (2) "How" we claim they "diverted"; (3) "How" we claim they "misappropriated"; (4) "How" we claim they "diverted" and "misappropriated". These last three numbered things are, manifestly, but one thing. We alleged that they diverted and misappropriated the corporation's funds and they now say that we must tell them how. It is not for a fiduciary who is sued for an accounting to require the complainant to set forth the particulars and details of the fiduciary's administration of the fund. It is rather for the fiduciary when once his accountability as such is established to furnish full disclosure before the Master. The gravamen of the suit is the fiduciary relationship and the fiduciaries' resulting accountability.

It is submitted that the motions are without the least merit.

It is also submitted that the motions were made solely for the purpose of delay. Your deponent in refusing the request of the solicitors for the defendants for extensions of time pointed out that the suit was by a Receiver and that it was highly important that the case should be tried before the adjournment of the Court for the summer recess and to the suggestion then made by the Solicitors for the defendants that the case could not be reached before that

[fol. 41] time pointed out that the complainant was entitled to a preference. Your deponent had prepared the necessary papers and was holding them awaiting the receipt of the answers in order that motion could immediately be made to place the case upon the calendar for trial under the preference rules applicable. Defendants' solicitors instead of answering have waited until the last day to apply for and obtain a ten days' extension to answer based upon this wholly unmeritorious motion. It should be noted that two of the defendants, viz. Maxime H. Furlaud and Kingston Corporation, represented by the same solicitors who represent the several defendants, found no difficulty in answering the original complaint which in the particlars now referred to in these motions does not vary in any respect whatsoever from the amended bill of complaint. The nature of the suit, the fact that the complainant is properly entitled to a speedy trial, the facts and circumstances surrounding the proceedings heretofore had and the wholly unmeritorious nature of the motions indicate clearly that the motions are made for the sole purpose of delay.

It is finally submitted that the motions should be denied; that the trial should be preferred and the case placed upon the day calendar in such position as to assure trial before the adjournment of the Court for the summer recess and the defendants required immediately to file their answers to the amended bill of complaint.

Ralph Royall.

Sworn to before me this 23rd day of May, 1932.
Florence Perea, Notary Public.

[fol. 42] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER DENYING MOTIONS TO REQUIRE COMPLAINANT TO MAKE FURTHER AND BETTER STATEMENT AS TO CLAIM—June 23, 1932.

On reading and filing the four orders to show cause herein, dated May 19, 1932, and the affidavits of Ira W. Hirshfield, sworn to May 19, 1932, annexed to said orders to show cause, and upon all the prior proceedings had

herein, and having heard Eppstein & Hirshfield (by Ira W. Hirshfield, of course) in support of the motions of defendants Maxime H. Furlaud, Chaucer Corporation, Byron Corporation and Kingston Corporation to require the complainant herein to make a further and better statement of [fol. 43] the nature of the claim and/or claims set forth in the amended bill of complaint as set forth in said orders to show cause, and having heard Ehrich, Royall, Wheeler & Walter, solicitors for the complainant herein (by Ralph Royall, of counsel) in opposition to said motions, and due deliberation having been had, and the Court having filed its opinion, dated June 17, 1832,

Now, on motion of Ehrich, Royall, Wheeler & Walter, solicitors for the complainant, it is

Ordered that said motions of defendants Maxime H. Furlaud, Chaucer Corporation, Byron Corporation and Kingston Corporation to require the complainant to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint be and the same hereby are denied, and that said defendants answer said amended bill within ten days after service of a copy of this order.

Francis G. Caffey, U. S. D. J.

[fol. 44] In United States District Court, Southern District of New York

[Title omitted]

Memorandum of Caffey, D. J.

I feel that care should be taken at this stage to avoid a ruling which would become the law of the case (Commercial Union v. Anglo South American Bank, 10 Fed. [2d] 937). I shall therefore not discuss the merits and shall confine myself to what I deem essential for disposition of the four motions.

I think that there is a clear single thread running throughout the Amended Complaint. In consequence, there is no justification for directing separation in the statement of causes of action. I think also that the allegations sufficiently meet the requirements of Equity Rule 25 and that,

at least prior to answer, there is no warrant for compelling a better statement under Rule 20.

Motions denied, with leave to defendants to answer within ten days after service of a copy of the order hereon.

Settle order on one day's notice.

Dated, June 17, 1932.

Francis G. Caffey, U.S. D. J.

[fol. 45] In United States District Court, Southern District of New York

[Title omitted]

Answer of Kingston Corporation

Kingston Corporation, for answer to the amended bill of complaint herein:

1. Admits the allegations of Paragraph "First" of the amended bill of complaint.

2. Denies any knowledge or information sufficient to form a belief as to whether complainant is a resident of the City of Pittsburgh and a resident and citizen of the Commonwealth of Pennsylvania, and admits the other allegations of paragraph "Second" of the amended bill of complaint.

3. With respect to the allegation of paragraph "Fourth" of the amended bill of complaint, defendant denies having information sufficient to form a belief with respect thereto and leaves the complainant to his proof thereof.

[fol. 46] 4. With respect to paragraph "Fifth" of the amended bill of complaint, defendant denies each and every allegation thereof except that it admits that on or about the 18th day of July, 1928, a corporation was organized and existed under the laws of the State of New York named "Furlaud & Company, Inc.", the name of which was later changed to "Furlaud, Reuter & Co., Incorporated" and later changed to "Winchelsea Holding Corporation", a certificate of dissolution of which was filed on the 27th day of October, 1931.

5. With respect to paragraph "Sixth" of the amended bill of complaint, defendant denies each and every allegation thereof except that it admits that Duquesne Gas Corporation was duly incorporated under the laws of the State of Pennsylvania and that it owned and operated natural gas wells and admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused the organization of Duquesne Gas Corporation; that Randolph C. Coleman, McLane Tilton and Frank A. Cabeen, Jr., acted for and on behalf of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc.; and that Otto E. Schuller, Thomas W. Duke, Henry T. Wynn and Charles C. Henderson were all employed by or acted on behalf of Winchelsea Holding Corporation then known as Furlaud & Company, Inc.

6. With reference to paragraph "Seventh" of the amended bill of complaint, defendant denies each and every allegation thereof but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused Duquesne Gas Corporation to authorize a first mortgage of Four million dollars ($4,000,000) securing an issue of [fol. 47] Four million dollars ($4,000,000) of first mortgage bonds of Duquesne Gas Corporation, and caused an indenture of One million dollars ($1,000,000) to be issued covering the issue of One million dollars ($1,000,000) of Convertible 6½% Secured Gold Notes, and caused the issuance of Six hundred and seventy-five thousand (675,000) shares of no par value Common Stock of Duquesne Gas Corporation.

7. With respect to paragraph "Eighth" of the amended bill of complaint, defendant denies each and every allegation contained therein but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., purchased from Duquesne Gas Corporation and others, certain bonds and notes of Duquesne Gas Corporation and resold some of the said bonds and notes to others.

8. With respect to paragraph "Ninth" of the amended bill of complaint, defendant denies each and every allegation contained therein.

9. With respect to paragraph "Tenth" of the amended bill of complaint, defendant denies each and every allega-

tion and alleges that all of the bonds, notes and stock of Duquesne Gas Corporation were issued in consideration of the payment to Duquesne Gas Corporation of sundry sums of money and/or the transfer to it of properties or other things of value of the fair, reasonable and/or appraised value of the amount of the bonds and/or notes issued and that immediately after the issuance of the said bonds, notes and stock Winchelsea Holding Corporation and/or defendants Furlaud, Reuter, Kingston Corporation, Byron Corporation and/or Chaucer Corporation and/or the nominees [fol. 48] of them or of one or more of them were the holders of all of the issued and outstanding stock of the said Duquesne Gas Corporation.

10. With respect to paragraph "Eleventh" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every sale of a bond or note of Duquesne Gas Corporation as alleged in the amended bill of complaint was made for the account of the Seller thereof who was the owner thereof and not for the account of Duquesne Gas Corporation.

11. With respect to paragraph "Twelfth" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every share of stock issued by the Duquesne Gas Corporation was properly issued by the said Duquesne Gas Corporation for a good and valuable consideration, and resold by the person, firm or corporation (or the nominee of the said person, firm or corporation) to whom the stock was originally issued, for the account of that person, firm or corporation and not for the account of Duquesne Gas Corporation.

12. With respect to paragraph "Thirteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

13. With respect to paragraph "Fourteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

14. With respect to paragraph "Fifteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

[fol. 49] 15. With respect to paragraph "Sixteenth" of the amended bill of complaint, defendant denies each and

every allegation thereof except that defendant admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., organized and was (through its nominees) the sole stockholders of Kingston Corporation, that Winchelsea Holding Corporation then known as Furlaud & Company, Inc. purchased from Duquesne Gas Corporation, Two million seven hundred thousand dollars ($2,700,000) of bonds and One million dollars ($1,000,000) of notes at a price of 90 for the bonds and 88 for said notes, and further admits that under date of April 7, 1930 a written paper called "Agreement of Reorganization between Duquesne Gas Corporation and Kingston Corporation of New Jersey" was duly signed and executed, and further admits that Krogg and Halporn were employees of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., and further admits that Kingston Corporation declared a dividend in kind to its stockholders of One Million three hundred thousand dollars ($1,300,000) in face amount of bonds of Duquesne Gas Corporation and Twenty-five thousand (25,000) shares of the capital stock of Duquesne Gas Corporation and further admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., subscribed and paid for One hundred and forty thousand (140,000) shares of stock of Duquesne Gas Corporation and paid therefor at the rate of fifty cents (50c.) per share, and further admits that the said Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., sold the major part of the One million three [fol. 50] hundred thousand dollars ($1,300,000) in face amount of bonds which were received by it from Kingston Corporation.

16. With respect to paragraph "Seventeenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

The defendant, without waiving any of the foregoing defenses and further answering said amended bill of complaint, alleges:

17. Upon information and belief, that the orginal subscribers to the capital stock of Duquesne Gas Corporation and each and every other person (or the person, persons,

firm, firms, corporation or corporations for whom it or they were acting) who, from the inception of Duquesne Gas Corporation until on or about May 15, 1930, was either a stockholder of the said company or a subscriber for stock of said company or in any way otherwise interested in the stock of the company then issued or thereafter to be issued, had full knowledge of the corporate transactions referred to in the amended bill of complaint and of all matters affecting the same and with such knowledge approved the corporate transactions referred to in the amended bill of complaint and from time to time re-elected the directors who had authorized the same and ratified and affirmed said transaction by their acquiescence thereto and that at a meeting of the stockholders of Duquesne Gas Corporation duly held on April 8, 1930, at which all of the issued and outstanding stock of the corporation was present in person or by proxy, all of the acts set forth in the amended bill of complaint [fol. 51] were, by unanimous vote, ratified and confirmed and that the defendants, Furlaud, Reuter, Kingston Corporation, Chaucer Corporation and/or Byron Corporation and/or Winchelsea Holding Corporation and/or their nominees owned and/or controlled, at all pertinent times mentioned in the amended bill of complaint all of the issued, outstanding and/or subscribed stock of Duquesne Gas Corporation.

Wherefore defendant prays that the amended bill of complaint be dismissed and it have such other and further relief as to the Court appears to be just.

Eppstein & Hirshfield, Solicitors for Kingston Corporation, Office & P. O. Address, 521 Fifth Avenue, Borough of Manhattan, City of New York.

(Verified on June 22, 1932, by Maxime H. Furlaud as President of Kinston Corporation.)

[fol. 52] In United States District Court, Southern District of New York

[Title omitted]

Answer of Maxime H. Furlaud

Maxime H. Furlaud, for answer to the amended bill of complaint herein:

1. Admits the allegations of Paragraph "First" of the amended bill of complaint.

2. Denies any knowledge or information sufficient to form a belief as to whether complainant is a resident of the City of Pittsburgh and a resident and citizen of the Commonwealth of Pennsylvania, and admits the other allegations of paragraph "Second" of the amended bill of complaint.

3. With respect to the allegation of paragraph "Fourth" of the amended bill of complaint, defendant denies having information sufficient to form a belief with respect thereto and leaves the complainant to his proof thereof.

[fol. 53] 4. With respect to paragraph "Fifth" of the amended bill of complaint, defendant denies each and every allegation thereof except that he admits that on or about the 18th day of July, 1928, a corporation was organized and existed under the laws of the State of New York named "Furlaud & Company, Inc.", the name of which was later changed to "Furlaud, Reuter & Co., Incorporated" and later changed to "Winchelsea Holding Corporation", a certificate of dissolution of which was filed on the 27th day of October, 1931.

5. With respect to paragraph "Sixth" of the amended bill of complaint, defendant denies each and every allegation thereof except that he admits that Duquesne Gas Corporation was duly incorporated under the laws of the State of Pennsylvania and that it owned and operated natural gas wells and admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc. caused the organization of Duquesne Gas Corporation; that Randolph C. Coleman, McLane Tilton and Frank A. Cabeen, Jr., acted for and on behalf of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc.; and that Otto E. Schuller, Thomas W. Duke, Henry T. Wynn and Charles C. Henderson were all employed by or acted on behalf of Winchelsea Holding Corporation then known as Furlaud & Company, Inc.

6. With reference to paragraph "Seventh" of the amended bill of complaint, defendant denies each and every allegation thereof but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused Duquesne Gas Corporation to authorize a first mortgage of

[fol. 54] Four million dollars ($4,000,000) securing an issue of Four million dollars ($4,000,000) of first mortgage bonds of Duquesne Gas Corporation, and caused an indenture of One million dollars ($1,000,000) to be issued covering the issue of One million dollars ($1,000,000) of Convertible 6½% Secured Gold Notes, and caused the issuance of Six hundred and seventy-five thousand (675,000) shares of no par value Common Stock of Duquesne Gas Corporation.

7. With respect to paragraph "Eighth" of the amended bill of complaint, defendant denies each and every allegation contained therein but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., purchased from Duquesne Gas Corporation and others, certain bonds and notes of Duquesne Gas Corporation and resold some of the said bonds and notes to others.

8. With respect to paragraph "Ninth" of the amended bill of complaint, defendant denies each and every allegation contained therein.

9. With respect to paragraph "Tenth" of the amended bill of complaint, defendant denies each and every allegation and alleges that all of the bonds, notes and stock of Duquesne Gas Corporation were issued in consideration of the payment to Duquesne Gas Corporation of sundry sums of money and/or the transfer to it of properties or other things of value of the fair, reasonable and/or appraised value of the amount of the bonds, and/or notes issued and that immediately after the issuance of the said bonds, notes and stock Winchelsea Holding Corporation and/or de- [fol. 55] fendants Furland, Reuter, Kingston Corporation, Byron Corporation and/or Chaucer Corporation and/or the nominees of them or of one or more of them were the holders of all of the issued and outstanding stock of the said Duquesne Gas Corporation.

10. With respect to paragraph "Eleventh" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every sale of a bond or note of Duquesne Gas Corporation as alleged in the amended bill of complaint was made for the account of the Seller thereof who was the owner thereof and not for the account of Duquesne Gas Corporation.

11. With respect to paragraph "Twelfth" of the amended bill of complaint, defendant denies each and every

allegation thereof and alleges that each and every share of stock issued by the Duquesne Gas Corporation was properly issued by the said Duquesne Gas Corporation for a good and valuable consideration, and resold by the person, firm or corporation (or the nominee of the said person, firm or corporation) to whom the stock was originally issued, for the account of that person, firm or corporation and not for the account of Duquesne Gas Corporation.

12. With respect to paragraph "Thirteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

13. With respect to paragraph "Fourteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

[fol. 56] 14. With respect to paragraph "Fifteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

15. With respect to paragraph "Sixteenth" of the amended bill of complaint, defendant denies each and every allegation thereof except that defendant admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., organized and was (through its nominees) the sole stockholder of Kingston Corporation, that Winchelsea Holding Corporation then known as Furlaud & Company, Inc. purchased from Duquesne Gas Corporation, Two million seven hundred thousand dollars ($2,700,000) of bonds and One million dollars ($1,000,000) of notes at a price of 90 for the bonds and 88 for said notes, and further admits that under date of April 7, 1930, a written paper called "Agreement of Reorganization between Duquesne Gas Corporation and Kingston Corporation of New Jersey" was duly signed and executed, and further admits that Krog and Halporn were employees of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., and further admits that Kingston Corporation declared a dividend in kind to its stockholders of One Million three hundred thousand dollars ($1,300,000) in face amount of bonds of Duquesne Gas Corporation and Twenty-five thousand (25,000) shares of the capital stock of Duquesne Gas Corporation, and further admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., sub-

scribed and paid for One hundred and forty thousand (140,000) shares of stock of Duquesne Gas Corporation and paid therefor at the rate of fifty cents (50c) per share, and further admits that the said Winchelsea Holding Cor-
[fol. 57] poration, then known as Furland & Company, Inc., sold the major part of the One million three hundred thousand dollars ($1,300,000) in face amount of bonds which were received by it from Kingston Corporation.

16. With respect to paragraph "Seventeenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

The defendant, without waiving any of the foregoing defenses and further answering said amended bill of complaint, alleges:

17. Upon information and belief, that the original subscribers to the capital stock of Duquesne Gas Corporation and each and every other person (or the person, persons, firm, firms, corporation or corporations for whom he or they were acting) who, from the inception of Duquesne Gas Corporation until on or about May 15, 1930 was either a stockholder of the said company or a subscriber for stock of said company or in any way otherwise interested in the stock of the company then issued or thereafter to be issued, had full knowledge of the corporate transactions referred to in the amended bill of complaint and of all matters affecting the same and with such knowledge approved the corporate transactions referred to in the amended bill of complaint and from time to time reelected the directors who had authorized the same and ratified and affirmed said transaction by their acquiescence thereto and that at a meeting of the stockholders of Duquesne Gas Corporation duly held on April 8, 1930 at which all of the issued and outstanding stock of the cor-
[fol. 58] poration was present in person or by proxy, all of the acts set forth in the amended bill of complaint were, by unanimous vote, ratified and confirmed and that the defendants, Furland, Reuter, Kingston Corporation, Chaucer Corporation and/or Byron Corporation and/or Winchelsea Holding Corporation and/or their nominees owned and/or controlled, at all pertinent times mentioned in the amended bill of complaint all of the issued, outstanding and/or subscribed stock of Duquesne Gas Corporation.

Wherefore defendant prays that the amended bill of complaint be dismissed and he have such other and further relief as to the Court appears to be just.

Eppstein & Hirshfield, Solicitors for Maxime H. Furlaud, Office & P. O. Address, 521 Fifth Avenue, Borough of Manhattan, City of New York.

(Verified on June 22, 1932, by the defendant Maxime H. Furlaud.)

[fol. 59] In United States District Court, Southern District of New York

[Title omitted]

Answer of Byron Corporation

Byron Corporation, for answer to the amended bill of complaint herein:

1. Admits the allegations of Paragraph "First" of the amended bill of complaint.

2. Denies any knowledge or information sufficient to form a belief as to whether complainant is a resident of the City of Pittsburgh and a resident and citizen of the Commonwealth of Pennsylvania, and admits the other allegations of paragraph "Second" of the amended bill of complaint.

3. With respect to the allegation of paragraph "Fourth" of the amended bill of complaint, defendant denies having information sufficient to form a belief with respect thereto and leaves the complainant to his proof thereof.

[fol. 60] 4. With respect to paragraph "Fifth" of the amended bill of complaint, defendant denies each and every allegation thereof except that he admits that on or about the 18th day of July, 1928, a corporation was organized and existed under the laws of the State of New York named "Furlaud & Company, Inc.", the name of which was later changed to "Furlaud, Reuter & Co., Incorporated" and later changed to "Winchelsea Holding Corporation", a certificate of dissolution of which was filed on the 27th day of October, 1931.

5. With respect to paragraph "Sixth" of the amended bill of complaint, defendant denies each and every allega-

tion thereof except that it admits that Duquesne Gas Corporation was duly incorporated under the laws of the State of Pennsylvania and that it owned and operated natural gas wells and admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc. caused the organization of Duquesne Gas Corporation; that Randolph C. Coleman, McLane Tilton and Frank A. Cabeen, Jr., acted for and on behalf of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc.; that Otto E. Schuller, Thomas W. Duke, Henry T. Wynn and Charles C. Henderson were all employed by or acted on behalf of Winchelsea Holding Corporation then known as Furlaud & Company, Inc.

6. With reference to paragraph "Seventh" of the amended bill of complaint, defendant denies each and every allegation thereof but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused Duquesne Gas Corporation to authorize a first mortgage of [fol. 61] Four million dollars ($4,000,000) securing an issue of Four million dollars ($4,000,000) of first mortgage bonds of Duquesne Gas Corporation, and caused an indenture of One million dollars ($1,000,000) to be issued covering the issue of One million dollars ($1,000,000) of Convertible 6½% Secured Gold Notes, and caused the issuance of Six hundred and seventy-five thousand (675,000) shares of no par value Common stock of Duquesne Gas Corporation.

7. With respect to paragraph "Eighth" of the amended bill of complaint, defendant denies each and every allegation contained therein but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., purchased from Duquesne Gas Corporation and others, certain bonds and notes of Duquesne Gas Corporation and resold some of the said bonds and notes to others.

8. With respect to paragraph "Ninth" of the amended bill of complaint, defendant denies each and every allegation contained therein.

9. With respect to paragraph "Tenth" of the amended bill of complaint, defendant denies each and every allegation and alleges that all of the bonds, notes and stock of Duquesne Gas Corporation were issued in consideration of the payment to Duquesne Gas Corporation of sundry

sums of money and/or the transfer to it of properties or other things of value of the fair, reasonable and/or appraised value of the amount of the bonds and/or notes issued and that immediately after the issuance of the said bonds, notes and stock Winchelsea Holding Corporation and/or defendants Furlaud, Reuter, Kingston Corporation, [fol. 62] Byron Corporation and/or Chaucer Corporation and/or the nominees of them or of one or more of them were the holders of all of the issued and outstanding stock of the said Duquesne Gas Corporation.

10. With respect to paragraph "Eleventh" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every sale of a bond or note of Duquesne Gas Corporation as alleged in the amended bill of complaint was made for the account of the Seller thereof who was the owner thereof and not for the account of Duquesne Gas Corporation.

11. With respect to paragraph "Twelfth" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every share of stock issued by the Duquesne Gas Corporation was properly issued by the said Duquesne Gas Corporation for a good and valuable consideration, and resold by the person, firm or corporation (or the nominee of the said person, firm or corporation) to whom the stock was originally issued, for the account of that person, firm or corporation and not for the account of Duquesne Gas Corporation.

12. With respect to paragraph "Thirteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

13. With respect to paragraph "Fourteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

14. With respect to paragraph "Fifteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

[fol. 63] 15. With respect to paragraph "Sixteenth" of the amended bill of complaint, defendant denies each and every allegation thereof except that defendant admits that Winchelsea Holding Corporation, then known as Furlaud

& Company, Inc. organized and was (through its nominees) the sole stockholder of Kingston Corporation, that Winchelsea Holding Corporation then known as Furlaud & Company, Inc., purchased from Duquesne Gas Corporation, Two million seven hundred thousand dollars ($2,700,000) of bonds and One million dollars ($1,000,000) of notes at a price of 90 for the bonds and 88 for said notes, and further admits that under date of April 7, 1930, a written paper called "Agreement of Reorganization between Duquesne Gas Corporation and Kingston Corporation of New Jersey" was duly signed and executed, and further admits that Krog and Halporn were employees of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., and further admits that Kingston Corporation declared a dividend in kind to its stockholders of One Million three hundred thousand dollars ($1,300,000) in face amount of bonds of Duquesne Gas Corporation and Twenty-five thousand (25,000) shares of the capital stock of Duquesne Gas Corporation, and further admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., subscribed and paid for One hundred and forty thousand (140,000) shares of stock of Duquesne Gas Corporation and paid therefor at the rate of fifty cents (50c) per share, and further admits that the said Winchelsea Holding Corporation, then known as Furlaud & Company, Inc. sold the major part of the One Million three hundred [fol. 64] thousand dollars ($1,300,000) in face amount of bonds which were received by it from Kingston Corporation.

16. With respect to paragraph "Seventeenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

The defendant, without waiving any of the foregoing defenses and further answering said amended bill of complaint, alleges:

17. Upon information and belief, that the original subscribers to the capital stock of Duquesne Gas Corporation and each and every other person (or the person, persons, firm, firms, corporation or corporations for whom it or they were acting) who, from the inception of Duquesne Gas Corporation until on or about May 15, 1930 was either a stockholder of the said company or a subscriber for stock

of said company or in any way otherwise interested in the stock of the company then issued or thereafter to be issued, had full knowledge of the corporate transactions referred to in the amended bill of complaint and of all matters affecting the same and with such knowledge approved the corporate transactions referred to in the amended bill of complaint and from time to time re-elected the directors who had authorized the same and ratified and affirmed said transaction by their acquiescence thereto and that at a meeting of the stockholders of Duquesne Gas Corporation duly held on April 8, 1930 at which all of the issued and outstanding stock of the corporation was present in person or by proxy, all of the acts set forth in the amended bill of complaint were, by unanimous vote, ratified and con-
[fol. 65] firmed and that the defendants, Furland, Reuter, Kingston Corporation, Chaucer Corporation and/or Byron Corporation and/or Winchelsea Holding Corporation and/or their nominees owned and/or controlled, at all pertinent times mentioned in the amended bill of complaint all of the issued, outstanding and/or subscribed stock of Duquesne Gas Corporation.

Wherefore defendant prays that the amended bill of complaint be dismissed and it have such other and further relief as to the Court appears to be just.

Eppstein & Hirshfield, Solicitors for Byron Corporation, Office & P. O. Address, 521 Fifth Avenue, Borough of Manhattan, New York City.

(Verified on July 2, 1932, by Byron Corporation, by Paul M. Coonrod, Secretary.)

[fol. 66] In United States District Court, Southern District of New York

[Title omitted]

Answer of Chaucer Corporation

Chaucer Corporation, for answer to the amended bill of complaint herein:

1. Admits the allegations of Paragraph "First" of the amended bill of complaint.

2. Denies any knowledge or information sufficient to form a belief as to whether complainant is a resident of the City of Pittsburgh and a resident and citizen of the Commonwealth of Pennsylvania, and admits the other allegations of paragraph "Second" of the amended bill of complaint.

3. With respect to the allegation of paragraph "Fourth" of the amended bill of complaint, defendant denies having information sufficient to form a belief with respect thereto and leaves the complainant to his proof thereof.

[fol. 67] 4. With respect to paragraph "Fifth" of the amended bill of complaint, defendant denies each and every allegation thereof except that it admits that on or about the 18th day of July, 1928, a corporation was organized and existed under the laws of the State of New York named "Furlaud & Company, Inc.", the name of which was later changed to "Furlaud, Reuter & Co., Incorporated" and later changed to "Winchelsea Holding Corporation", a certificate of dissolution of which was filed on the 27th day of October, 1931.

5. With respect to paragraph "Sixth" of the amended bill of complaint, defendant denies each and every allegation thereof except that it admits that Duquesne Gas Corporation was duly incorporated under the laws of the State of Pennsylvania and that it owned and operated natural gas wells and admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused the organization of Duquesne Gas Corporation; that Randolph C. Coleman, McLane Tilton and Frank A. Cabeen, Jr., acted for and on behalf of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc.; and that Otto E. Schuller, Thomas W. Duke, Henry T. Wynn and Charles C. Henderson were all employed by or acted on behalf of Winchelsea Holding Corporation then known as Furlaud & Company, Inc.

6. With reference to paragraph "Seventh" of the amended bill of complaint, defendant denies each and every allegation thereof but admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., caused Duquesne Gas Corporation to authorize a first mortgage [fol. 68] of Four million dollars ($4,000,000) securing an issue of Four million dollars ($4,000,000) of first mortgage

bonds of Duquesne Gas Corporation, and caused an indenture of One million dollars ($1,000,000) to be issued covering the issue of One million dollars ($1,000,000) of Convertible 6½% Secured Gold Notes, and caused the issuance of Six hundred and seventy five thousand (675,000) shares of no par value Common Stock of Duquesne Gas Corporation.

7. With respect to paragraph "Eighth" of the amended bill of complaint, defendant denies each and every allegation contained therein but admits that Winchelsea Holding Corporation, then known as Furland & Company, Inc., purchased from Duquesne Gas Corporation and others, certain bonds and notes of Duquesne Gas Corporation and resold some of the said bonds and notes to others.

8. With respect to paragraph "Ninth" of the amended bill of complaint, defendant denies each and every allegation contained therein.

9. With respect to paragraph "Tenth" of the amended bill of complaint, defendant denies each and every allegation and alleges that all of the bonds, notes and stock of Duquesne Gas Corporation were issued in consideration of the payment to Duquesne Gas Corporation of sundry sums of money and/or the transfer to it of properties or other things of value of the fair, reasonable and/or appraised value of the amount of the bonds and/or notes issued and that immediately after the issuance of the said bonds, notes and stock Winchelsea Holding Corporation and/or defend- [fol. 69] ants Furland, Reuter, Kingston Corporation, Byron Corporation and/or Chaucer Corporation and/or the nominees of them or of one or more of them were the holders of all of the issued and outstanding stock of the said Duquesne Gas Corporation.

10. With respect to paragraph "Eleventh" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every sale of a bond or note of Duquesne Gas Corporation as alleged in the amended bill of complaint was made for the account of the Seller thereof who was the owner thereof and not for the account of Duquesne Gas Corporation.

11. With respect to paragraph "Twelfth" of the amended bill of complaint, defendant denies each and every allegation thereof and alleges that each and every share of stock

issued by the Duquesne Gas Corporation was properly issued by the said Duquesne Gas Corporation for a good and valuable consideration, and resold by the person, firm or corporation (or the nominee of the said person, firm or corporation) to whom the stock was originally issued, for the account of that person, firm or corporation and not for the account of Duquesne Gas Corporation.

12. With respect to paragraph "Thirteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

13. With respect to paragraph "Fourteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

[fol. 70] 14. With respect to paragraph "Fifteenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

15. With respect to paragraph "Sixteenth" of the amended bill of complaint, defendant denies each and every allegation thereof except that defendant admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., organized and was (through its nominees) the sole stockholders of Kingston Corporation, that Winchelsea Holding Corporation then known as Furlaud & Company, Inc., purchased from Duquesne Gas Corporation, Two million seven hundred thousand dollars ($2,700,000) of bonds and One million dollars ($1,000,000) of notes at a price of 90 for the bonds and 88 for said notes, and further admits that under date of April 7, 1930, a written paper called "Agreement of Reorganization between Duquesne Gas Corporation, then known as Furlaud & Company, Inc., and furduly signed and executed, and further admits that Krog and Halporn were employees of Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., and further admits that Kingston Corporation declared a dividend in kind to its stockholders of One million three hundred thousand dollars ($1,300,000) in face amount of bonds of Duquesne Gas Corporation and Twenty-five thousand (25,000) shares of the capital stock of Duquesne Gas Corporation, and further admits that Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., subscribed and paid for One hundred and forty thousand

(140,000) shares of stock of Duquesne Gas Corporation and paid therefor at the rate of fifty cents (50¢) per share, and [fol. 71] further admits that the said Winchelsea Holding Corporation, then known as Furlaud & Company, Inc., sold the major part of the One million three hundred thousand dollars ($1,300,000) in face amount of bonds which were received by it from Kingston Corporation.

16. With respect to paragraph "Seventeenth" of the amended bill of complaint, defendant denies each and every allegation thereof.

The defendant, without waiving any of the foregoing defenses and further answering said amended bill of complaint, alleges:

17. Upon information and belief, that the original subscribers to the capital stock of Duquesne Gas Corporation and each and every other person (or the person, persons, firm, firms, corporation or corporations for whom it or they were acting), who, from the inception of Duquesne Gas Corporation until on or about May 15, 1930, was either a stockholder of the said company or a subscriber for stock of said company or in any way otherwise interested in the stock of the company then issued or thereafter to be issued, had full knowledge of the corporate transactions referred to in the amended bill of complaint and of all matters affecting the same and with such knowledge approved the corporate transactions referred to in the amended bill of complaint and from time to time re-elected the directors who had authorized the same and ratified and affirmed said transaction by their acquiescence thereto and that at a meeting of the stockholders of Duquesne Gas Corporation duly held on April 8, 1930, at which all of the issued and outstand-[fol. 72] ing stock of the corporation was present in person or by proxy, all of the acts set forth in the amended bill of complaint were, by unanimous vote, ratified and confirmed and that the defendants, Furlaud, Reuter, Kingston Corporation, Chaucer Corporation and/or Byron Corporation and/or Winchelsea Holding Corporation and/or their nominees owned and/or controlled, at all pertinent times mentioned in the amended bill of complaint all of the issued, outstanding and/or subscribed stock of Duquesne Gas Corporation.

Wherefore defendant prays that the amended bill of complaint be dismissed and it have such other and further relief as to the Court appears to be just.

Eppstein & Hirshfield, Solicitors for Chaucer Corporation, Office & P. O. Address, 521 Fifth Avenue, Borough of Manhattan, City of New York.

(Verified on July 2, 1932 by Paul M. Coonrod, as secretary of Chaucer Corporation.)

[fol. 73] In United States District Court, Southern District of New York

In Equity No. E. 66-185

George W. McCandless, as Receiver of Duquesne Gas Corporation, Plaintiff,

vs.

Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation,

Statement of Evidence

Before Hon. John C. Knox, D. J.

Appearances:

Ehrich, Royall, Wheeler & Walter, Esqs., Solicitors for Complainant (Ralph Royall, M. W. Ehrich, Wm. A. Magee, Clark Miller, Esqs., of Counsel).

Eppstein & Hirshfield, Esqs., Solicitors for all of the Defendants with the exception of Carlos Reuter (not served) (Ira W. Hirshfield, Esq., of Counsel).

George W. McCandless, called as a witness by the complainant, testified as follows:

Direct examination.

By Mr. Royall:

I am the plaintiff in this suit, and I was appointed Re- [fol. 74] ceiver of the Duquesne Gas Corporation by the

United States District Court for the Western District of Pennsylvania on January 19th, 1932.

I was appointed in the suit in which the Central Hanover Bank & Trust Company, as Trustee under the first mortgage of the Duquesne Gas Corporation, was plaintiff, combined with another suit that was brought in the same Court.

Q. Thereafter did you apply for and obtain authority from the Court to bring this suit?

Mr. Hirshfield: May I object to that, your Honor?

The Court: What is the ground of your objection?

Mr. Hirshfield: The ground of my objection is that the order itself is the best evidence of what is contained therein. I might say at this point that I intend to raise the point in the course of this trial that the trustee had no authority to bring the suit in the particular action under which he was appointed.

Mr. Royall: What disposition does your Honor make of the objection?

The Court: You better have the order.

By Mr. Royall:

Q. Were you thereafter appointed ancillary receiver by this District Court?

A. I did not get the question.

Q. I say, were you thereafter appointed ancillary receiver in this district?

A. Yes.

Q. Were you there also authorized to bring suit?

Mr. Hirshfield: I make the same objection.

[fol. 75] The Court: The order would be the best evidence.

Mr. Royall: I ask that the record in the ancillary proceedings in this matter be marked in evidence.

The Court: I will take the order appointing the witness as ancillary receiver—that is, if it shows it, I will take it.

Mr. Royall: I ask that the file be received in evidence.

(Document deemed marked Plaintiff's Exhibit 1.)

CHARLES C. NUSS, called as a witness by the complainant, testified as follows:

Direct examination.

By Mr. Royall:

At the time of the receivership I was President of the Duquesne Gas Corporation. I, my father and some others together were associated in the ownership of the Nuss property.

I first met Mr. Reuter in January, 1930, in Pittsburgh. He said he was interested in buying gas properties and that he had heard we had some property, and that he would like to arrange a sales agreement whereby he might acquire it.

Q. Will you tell us briefly, in your own way, what your further contacts about that time were with Mr. Reuter, and what next happened?

A. Do you mean just in regard to my own property?

Q. In regard to any of your activities with respect to this whole affair with Mr. Reuter?

Mr. Hirshfield: May I object to this, your Honor? Reuter is a defendant who has not been served.

[fol. 76] The Court: Was there a concert of action between all of these parties including Reuter?

Mr. Royall: Oh, yes, Reuter and Furland & Company were together in the enterprise. It was called Furland & Co.; later on it became Furland & Reuter. It seems that Reuter was so good, that he deserved to have his name in the firm.

The Court: All right.

Mr. Hirshfield: Exception.

Mr. Reuter said that he had heard of other properties in that territory that he might desire to acquire and asked about the Behm property and other properties. Mr. Behm and I discussed our properties and the prices for our properties. Mr. Reuter asked that I either accompany some of his employees or go myself to find out whether other property owners would be interested in drawing up sales agreements. We agreed on the price of $660,000 for my property, $200,000 for Mr. Behm's property and for a certain other property known as the Garrison property, $120,000.

Q. I show you a paper and ask you if this is the sales agreement referred to by you, relating to the Nuss property (handing paper)?

A. This is the sales agreement or option agreement.

Mr. Royall: I offer it in evidence. I have had a summary of this made, and when we get through, we can put in a summary.

Mr. Hirshfield: I object to the introduction of this as being immaterial and not binding on Furland personally.

The Court: I will take it for the time being, and if it [fol. 77] does not become material, at a later time you may move to strike it out, but in the meantime, I will take it and allow the case to go on.

Mr. Hirshfield: Exception.

(Marked Plaintiff's Exhibit No. 2.)

Plaintiff offered in evidence Plaintiff's Exhibit No. 3, being an agreement dated January 7, 1930, between Daniel Ritter, as purchaser, and Henderson Oil & Gas Co. with an assignment by Ritter to the Kingston Corporation, the purchase price being $165,000.

Plaintiff offered in evidence Plaintiff's Exhibit No. 4, being an agreement dated December 27, 1929, between Starr and Kingston Corporation, as purchaser, affecting the property known as Trafford Oil & Gas Co., the purchase price of which was $815,000.

Plaintiff offered in evidence Plaintiff's Exhibit No. 5, being an agreement dated January 6, 1930, between Ritter and Wally covering the property known as the Wally property, the consideration recited being $135,000 together with an assignment by Ritter to the Kingston Corporation.

Plaintiff offered in evidence Plaintiff's Exhibit No. 6, consisting of two agreements dated February 5, 1930, between Kingston Corporation and Victor D. Behm and wife covering the Behm properties and reciting an aggregate purchase price of $200,000.

Plaintiff offered in evidence Plaintiff's Exhibit No. 7, being an agreement dated January 2, 1930, between Daniel [fol. 78] Ritter and I. T. Campbell, covering property known as the Campbell property, and reciting a consideration of $135,000 to which is attached an assignment by Ritter to the Kingston Corporation.

Plaintiff offered in evidence Plaintiff's Exhibit No. 8, consisting of an agreement dated February 5, 1930, between Kingston Corporation and one Garrison, reciting a consideration of $120,000 covering the sale of the Garrison property.

Plaintiff offered in evidence Plaintiff's Exhibit No. 9, being an agreement dated January 4th, 1930, between Ritter and A. J. Degenther, reciting a consideration of $125,000 covering property known as the Byers property, to which is attached an assignment thereof to the Kingston Corporation.

Plaintiff offered in evidence Plaintiff's Exhibit No. 10, being an agreement between Ritter and one Gallagher, dated January 8, 1930, reciting a consideration of $185,000 covering property known as the Gallagher property, and is assigned by Ritter to the Kingston Corporation.

The witness identified the foregoing Plaintiff's Exhibits 3-10 inclusive.

Objections were made to the introduction of all of the foregoing on the ground that the said evidence was immaterial, and upon the further ground that the said evidence was not binding upon the defendant Maxime H. Furlaud.

Objections overruled, and exceptions taken.

[fol. 79] Q. Have you prepared a schedule of these contracts, showing the purchase prices, the appraised values, dates of sale, assignment of sales agreements, and so forth and so on, for the convenience of the Court?

A. I did.

Q. I show you a paper and ask you if that is the schedule that you refer to (handing witness)?

A. It is.

Q. Is it correct?

A. Yes.

Mr. Royall: I ask that it be marked in evidence, as a summary of matters already in evidence, simply for the convenience of the Court.

Mr. Hirshfield: I object to that, your Honor, upon two grounds. First, it is entirely immaterial, and second, it is not binding upon Furlaud.

By the Court:

Q. This is a schedule that is made up of these papers that have just been offered in evidence?

A. Yes.

The Court: I will take it, simply as a compilation.

Mr. Hirshfield: Your Honor, I understand there are some compilations as to appraisals. I suppose you do not refer to them.

The Court: It is a schedule of these various option agreements.

Mr. Royall: I did say something about appraisal.

The Court; As I understand, this is simply a summary of what has already been put in.

[fol. 80] Mr. Hirshfield: I desire to raise a question sharply on the matter of the appraisal.

The Court: I will take it simply as a compilation of what is already in evidence. That is the only bearing it will have.

(Marked Plaintiff's Exhibit No. 11.)

Thereafter, Mr. Reuter informed us, especially Behm and myself, that it would be necessary to have an extension drawn extending the time when payments would be made against the property. This extension agreement was made between me and the Kingston Corporation. At that time, $15,000 was paid to me and I was to secure the option on the Garrison property so as to bind me and to bind the Garrison option.

Q. Have you obtained from the files of the Duquesne Gas Corporation any similar extension agreements, so-called?

A. I did.

Mr. Royall: I offer in evidence the so-called extension agreement between Nuss and the Kingston Corporation dated the 3rd day of March, 1930.

Mr. Hirshfield: I make the same objection to that, your Honor.

The Court: Same ruling.

Mr. Hirshfield: Exception.

(Marked Plaintiff's Exhibit 12.)

Mr. Royall: I am willing to stipulate that the same objection may be taken, or considered to be taken, to all this line of testimony.

The Court: This is just the chain of title, I take it, to [fol. 81] these properties that came in.

Mr. Royall: I will save my friend's time and the Court's time by stipulating that he be deemed to have taken an objection to this whole line of testimony and an exception to the Court's ruling.

The Court: Very well.

Plaintiff offered in evidence Plaintiff's Exhibit No. 13, being a paper dated March 3rd, 1930, covering an extension of the Behm option and reciting a consideration of $4,000.

Plaintiff offered in evidence Plaintiff's Exhibit No. 14, being an extension signed by Garrison and others, dated March 3rd, and reciting as consideration for the extension of the option the payment of the sum of $2,000.

Those are all the extension agreements that I was able to produce from the files.

All of the deeds covering the nine properties were delivered on April 9th.

About the 10th of March we received a letter from the Kingston Corporation which was marked "Plaintiff's Exhibit No. 15", being a letter dated March 12th from Kingston Corporation, addressed to Mr. Nuss and others.

Plaintiff offered in evidence Plaintiff's Exhibit No. 16, being a letter addressed by Mr. Schuller, as Vice-President of Kingston Corporation to Mr. Garrison and others dated March 12th.

Plaintiff offered in evidence Plaintiff's Exhibit No. 17, [fol. 82] being a letter addressed to Mr. James S. Gallagher, owner of the Gallagher property.

Plaintiff offered in evidence Plaintiff's Exhibit No. 18, being a notice dated March 14th, 1930, signed by Schuller, as Vice-President of Kingston Corporation, stating that Kingston Corporation elects to proceed in accordance with the agreement, and also recites the delivery by Kingston to Nuss of a check for $15,000 of which $2,000 is to be paid to Garrison on or before March 15th.

Mr. Royall: I think we might, in order to save time, Mr. Hirshfield, agree that the files disclose similar letters addressed by Mr. Schuler, vice-president of Kingston, to Garrison, in the case of Garrison property, reciting $2000 had

been delivered to Mr. Nuss for him, and a letter to Degenther, being a representative of the Byers property; a letter to Gallagher, a letter to Campbell, a letter to Behm, Starr and Wally, and that is to be taken for granted, for the purposes of the case, that that arrangement was made for the entire list of nine properties—right?

Mr. Hirshfield: Right.

A deed or indenture of conveyance of my gas leases was prepared by the purchasers and deposited in escrow, in the Citizens National Bank of Washington, Pa., and the vendors were procured to execute the document of conveyance. All these papers were deposited in escrow in that bank under an understanding that they were to be delivered to the Duquesne Gas Corporation together with a deed upon my receiving the balance of the purchase price.

[fol. 83] Mr. Royall: The documents in question are powers of attorney from Thompson et al., to yourself and another. An assignment from yourself and wife—from J. B. Nuss and wife to Duquesne Gas Corporation of certain leaseholds; a further assignment from the same to the Duquesne Gas Corporation of certain leaseholds; seven assignments of gas sales contracts to Duquesne Gas Corporation executed by the same; transfer order on Southwest Pennsylvania Pipe Lines, dated March 11th, 1930, from J. B. Nuss and C. C. Nuss as trustees, to Duquesne Gas Corporation; and transfer order on Southwest Pennsylvania Pipe Lines, signed by J. B. Nuss and C. C. Nuss, trustees, to Duquesne Gas Corporation.

For the purpose of the record, if I may, in order to make the picture complete, state the substance of this—I see Mr. Hirshfield is looking over my shoulder to see that I make no mistake——

Mr. Hirshfield: Are you offering that in evidence?

Mr. Royall: I will offer it in evidence, yes.

Mr. Hirshfield: I have the same objection to this as the others.

The Court: The same ruling.

Mr. Hirshfield: Exception.

(Marked Plaintiff's Exhibit 19.)

Similar arrangements were made in respect of all the nine constituent properties through other local banks conveniently situated for the purpose.

The deeds recited in those letters as deposited were de-
[fol. 84] posited. They were deeds of conveyance running to the Duquesne Gas Corporation, as grantee, and were intended to convey to the Duquesne Gas Corporation the properties described in the deeds, the subject matter of the various sales. Similar deeds were delivered to the other escrow depositories with respect to all the other nine transactions.

Q. Mr. Nuss, are you an engineer by profession?
A. Do you mean at the present time, or have I been?
Q. Have you been?
A. Yes, I have been.
Q. Are you a graduate engineer, that is to say, have you had a technical education?
A. Yes, sir.
Q. Where?
A. I received a B.S. degree from W. & J. College in 1914.
Q. W. & J. means Washington & Jefferson?
A. Washington & Jefferson.
Q. Thereafter did you practice the profession of engineer?
A. Yes, sir.
Q. For how long a period of years?
A. For eleven years.
Q. Now, at the time of the organization of the Duquesne Gas Corporation, you and other members of your family were in business, the nature of which was the developing of gas wells as an enterprise of your own, isn't that so?
A. Yes.
Q. How long have you been active as a practical gas man, as an owner and developer?
A. For about eight years—eight to ten years.
Q. Have you bought gas leases and other gas properties?
A. I just bought leases.
Q. You bought gas leases. Well these are gas leases; that is what Duquesne owns, were gas leases?
A. There were no producing wells.
[fol. 85] Q. Even with a producing well on it, a gas lease is still a gas lease, isn't it?
A. It is termed as such, yes.
Q. In fact, it is.
A. It is an oil and gas lease, to state it correctly.

Q. You are familiar with the values of such properties, aren't you?

A. Yes, sir.

Q. And you are familiar with all these properties, the Nuss property, the Gallagher property and all of them in this whole group of property in the Duquesne Gas Corporation matter?

A. Yes.

Q. You are, in fact, now the general manager of the receiver in conducting these properties?

A. Yes.

Q. And have you been active in the Duquesne Gas Corporation ever since it acquired the properties, haven't you?

A. Yes.

Q. And you continued so for the corporation and since the receivership for the receiver, isn't that so?

A. Yes.

Q. And in that way, you are familiar with all these properties, are you not?

A. Yes.

Q. What, in your opinion, is the fair value of these properties as at——

Mr. Hirshfield: I object.

Mr. Royall: Wait until I finish my question. I know you want to object, and I will give you a chance to.

Mr. Hirshfield: Very well.

Q. (Continuing.) What, in your opinion, is the fair value of these properties as at about January to April of 1930?

Mr. Hirshfield: May I object to that, your Honor?

[fol. 86] Mr. Royall: I mean the fair market value.

Mr. Hirshfield: I object to that, your Honor, on two grounds. First, Mr. Nuss is not qualified as an expert. As he testified himself, he never bought a lease with a producing well on it, and inasmuch as a great many of these have producing wells on them, I must object to his testimony on that ground.

I object to it on the further ground of immateriality. It has absolutely no bearing on this case, what the values of these properties were, whether they were worth one dollar or one billion dollars. Certainly there is no allegation in the pleadings as to any particular value or lack of value of these wells.

The Court: What is the materiality or relevancy of the value of the property as of that date, over a year after what was paid for them?

Mr. Royall: The question does not come to the value over what they were paid—maybe they were not paid as much as they should have been paid—it seems to me, this being an equity case, it is certainly an essential part of this whole picture to know what this corporation got out of this thing. I suppose if your Honor were satisfied that this corporation really was not interested in what went on here and really got several million dollars worth of property——

The Court: The question here, as to the value of the property, as of about the time they were taken over, is one which might be very material if it were charged in the com-[fol. 87] plaint or the constituent part of your case that Furland & Company or the four defendants from whom you seek a recovery, took over these properties at grossly excessive values knowing they were worth much less than the amount they paid.

Mr. Royall: Your Honor, that is the theory of our case. We claim this, that these promoters took this four million dollars from the public for the bonds, plus a million dollars from the public for the notes and they were to use it and they were bound to use it for the benefit of the corporation.

The Court: If they exercised good faith in making the purchases, believing the properties would be worth this sum of money, there would be no fraud, as far as that was concerned. That might even be a fair value for the property—still, intent to perpetrate a fraud by floating upon this property, which let us say for the purpose of argument were all in bad faith—a large bond issue quite beyond the reasonable market value of the properties and pocketed the difference between what was required to take up the properties and the sum that they sold or realized upon the bonds——

Mr. Hirschfield: That is not pleaded in this case, your Honor.

Mr. Royall: Yes, it is.

The Court: Very well, let him see whether it is, so that we can get along. I do not see at the present time how that valuation would have very much to do with this case at this time.

[fol. 88] Mr. Royall: I am sure I will be able to convince your Honor that it is quite material.

Mr. Hirshfield: May I have an exception to your Honor's ruling?

The Court: Oh, yes.

The Witness: The fair market value, in my opinion, at that time was about $2,700,000.

By the Court:

Q. And what was the aggregate amount paid?

A. Two million five hundred thousand dollars—that is from memory.

Mr. Royall: This shows the amount that was paid, from this paper, $2,572,989.

By Mr. Royall:

Q. Now, Mr. Nuss, you testified that the property which you turned over was put in, and you received for it the sum of $660,000?

A. Yes.

Q. And your property became the subject of appraisal for the purchase of a bond issue, did it not? It became the subject of an appraisal, didn't it?

A. Yes, it did become the subject of an appraisal.

Q. Which appraisal was reflected in the statements contained in the bond issue, isn't that so?

A. Yes.

Q. And what values did your properties get put into that appraisal?

Mr. Hirshfield: I again make the same objection. I do not see how that is in any way material to any issue raised here.

[fol. 89] The Court: What is the source of his knowledge?

Mr. Royall: He has seen the appraisal.

The Court: I know, but that is hearsay evidence. That isn't direct evidence. It doesn't appear in the books of the corporation anywhere?

Mr. Royall: Yes, the books of the corporation carry the appraisals on the property.

The Court: Or the statement of the prospectus?

Mr. Royall: Yes, the prospectus.

The Court: But the prospectus does not break down?

Mr. Royall: The prospectus does not, but the appraisal breaks down.

The Court: All right, I will take it if you know.

Mr. Hirshfield: Exception.

Q. Will you answer the question?

A. It reports the appraised value of my property was $2,500,000.

By the Court:

Q. What did you think it was worth at that time?.

A. $660,000.

Q. You got full value for it?

A. Well, I considered that it was worth $800,000, but I thought he was entitled to the difference, so I sold it for $660,000.

Q. How many gas wells did you have on that property?

A. I had 17, I believe, and three drilling that were simultaneously turned over.

Q. How many feet of gas were you producing then?

[fol. 90] A. 700 million feet, or $140,000 at 20 cents.

Q. You were selling your gas to manufacturers?

A. I was selling manufacturers or their subsidiary companies that were affiliated with them—I was selling approximately 700 million feet a year.

Mr. Hirshfield: And may I say to your Honor that I was totally unprepared for this sort of testimony and I am not in any way prepared to controvert any of his testimony on that, because it did not seem to me from the pleadings that it could b brought out.

The Court: I will take it for the present. I am not certain at this time whether it is proper, but later I will entertain a motion to strike it out.

Mr. Hirshfield: I submit on the pleadings it has nothing to do with the case, and I think your Honor will agree with me when we come to consider the law of the case.

(Recess until 2:30 P. M.)

Afternoon Session

Charles C. Nuss, resumed the stand.

Direct examination.

By Mr. Royall (continued):

Q. Now, what is the transaction, Mr. Nuss, involving, the transfer by you, without consideration of some 14,000 acres of undeveloped land?

A. There was a transfer.

[fol. 91] Q. Tell us about that transaction.

A. Included in the sale of my property, there was 14,000 acres of undeveloped territory——

Q. Was this a lease subject to some stipulated annual payment?

A. It was a lease contingent upon a royalty basis of one-eighth of the proceeds of all gas sold, with a stipulation that one well be drilled within six months from the date of the lease, and wells to be drilled so often thereafter, in order to hold the lease in good standing.

Q. Would a lease like that to be sold or transferred generally have a market value, some market value?

A. Ordinarily, acreage of that sort is usually sold for a nominal price per acre, ranging from one dollar to two dollars, and maybe in a good sized block, it may be worth $5.00.

Q. But you say this was turned over by you without any additional consideration?

A. Yes.

Q. How did that item of 14,000 acres of undeveloped land appear in the appraisal? What value was assigned to it in the appraisal by the so-called experts?

Mr. Hirshfield: I again object to the use of Mr. Nuss as an expert, and I again object to the introduction of any testimony whatsoever along this line.

The Court: Do you object to the sum which he gives, which was recorded by these people who made the appraisal?

Mr. Hirshfield: Not the result that was given, but after all, this is leading up to his own estimate of value.

The Court: The same ruling.

Mr. Hirshfield: Exception.

Q. Will you answer the question?

A. It was given a value of $840,000.

[fol. 92] Q. In other words, Mattison, Davey & Winters, experts who appraised a part of the property, including your properties, used as a factor in building up your grand total of $5,100,000, the sum of $840,000 as the value for this property which you have last mentioned, which was turned over without consideration by you?

A. They did.

Q. The property was wholly undeveloped, was it?
A. Yes.

By the Court:

Q. Where did it lie?
A. It was in Preston County, West Virginia, and probably a part in Monongalia County.

By Mr. Royall:

Q. What was that based on, a valuation of future potentialities, was that the idea?
A. It was an estimate of future income or earnings from that property.
Q. Based upon the assumption that it could be drilled——

Mr. Hirshfield: Your Honor, I object again to this testimoney.

The Court: I suppose he cannot tell what the basis of the value was. It was undeveloped land. You are asking him to tell you the values which were placed upon these properties by someone who was retained by the Duquesne Gas Company.

Mr. Royall: By Furlaud.

The Court: If it is in the books, that is the best evidence but just as a matter if convenience, I will let him state.

[fol. 93] Mr. Hirshfield: I want to object to that. I want them to offer it if they are going to refer to it.

Mr. Royall: Just a minute on that. Their circular refers to the fact that Mattison, Davey & Winters placed a certain value on the property of $5,100,000; also other properties at $1,700,000. They plead that the properties were worth that. Now, we say if they want to rely upon these appraisals in this case as the evidence of value——

Mr. Hirshfield: Just where do we plead it?

Mr. Royall: Do you want me to show you that?

Mr. Hirshfield: Yes.

Mr. Royall: All right, "Defendants allege that all the bonds, notes and stock of the Duquesne Gas Corporation were issued in consideration of the payment to the Duquesne Gas Corporation of certain sums of money and transfer to it of properties and other things of the value, the fair and reasonable appraised value of the bonds and notes issued——

The Court: Gentlemen, I think you are wasting time, as far as that is concerned. You are now offering—if you do offer the books showing this appraisal, as being appraised on the actual value, you are simply offering it, as I understand it, if you decide to do so, to indicate what they did say was the value, without any endorsement of your client of that value. Now, it seems to me that the better thing for you to do is, with that limitation, to offer what the ap- [fol. 94] praisers show rather than do it indirectly through the method of asking the witness who has seen the appraisal on the books.

Mr. Royall: Well, your Honor, my proof is a little out of order, but I thought while I had this witness on the stand, I would ask him about that, but later on, and very soon, by a witness who will be called, I will prove it with these circulars.

The Court: All right, I don't know just what it is you have in mind, of course.

Mr. Royall: I think I have really finished with this witness and I was just taking up the argument that my friend presented, and at this time I am simply answering his question. I think the witness answered my question, however. There is something that I omitted in this chain, if your Honor will permit me.

The Court: All right.

Plaintiff offered in evidence a photostatic copy of a draft drawn by the Citizens National Bank of Washington, Pa., upon the Equitable Trust Company of New York, for $647,000 under date of April 1st, 1930. On the back it shows that it was paid on April 9th, 1930.

Mr. Hirshfield: I object, not on the ground that it is a photostatic copy, but on the same ground of incompetency.

Mr. Royall: All the way through, I told you that I would concede that you have a general objection to all of this testimony.

Mr. Hirshfield: I am not objecting on the ground that it is a photostatic copy, but on the previous grounds stated. [fol. 95] The Court: Yes, you may have an exception.

Mr. Royall: I offer it in evidence.

(Marked Plaintiff's Exhibit No. 20.)

Similar drafts were drawn by local banks in and about the Pittsburgh region with respect to the escrow arrangements covering the balance of the purchase price involved in the nine transactions.

Cross-examination.

By Mr. Hirshfield:

There is no question that those people who sold the property, who made the contracts with Kingston, received every cent of the money that they bargained for or expected to get.

Subsequent to the making of my contract with Kingston Corporation, the drilling on my property netted a seven million foot well. That was a very good well, among the best brought in in recent years. That was on my farm.

By Mr. Hirshfield:

Q. At the time you made the contract, you were drilling that well?

A. Yes, sir, I had already signed the sales agreement.

Q. And it was brought in subsequent——

A. Subsequent to the signing.

Q. So at the time that this contract was made, your property had a value of x dollars, we will say?

A. Yes, sir.

Q. On April 9th, did it or not have added value by reason of bringing in this tremendous well?

A. In my opinion, no, because in those reserves that was admitted as being there.

[fol. 96] Q. In other words, you were so certain ahead of time——

A. I didn't put those figures on it.

Q. Ever gotten a dry well, Mr. Nuss?

A. Yes, sir, certainly.

Q. So when you say that they were calculated in advance, you know that calculations are one thing and the actual bringing in of a tremendous well of that sort is another thing?

A. That is a fact.

Q. You never bought or sold any properties except the sales of your own property that had wells on it?

A. I bought oil and gas leases.

Q. But without wells, unproven, wild-cat——

A. Just unoperated acres.

Q. Practically wild-cat acreage, or would you say unproven, is there a distinction?

A. There is, in my opinion.

Q. But you had not had any experience in buying and selling any proven wells?

A. Except in my own use.

By the Court:

Q. Is a proven territory that which lies in certain off-set wells?

A. I would make a distinction there, yes.

Q. Wild-cat territory is a new territory, is that it?

A. Where there is nothing drilled or anything disclosed to indicate that there might be gas or anything.

Q. You testified before that you first met Mr. Reuter in, I think you said, January or February of 1930?

A. Yes, sir.

Q. Is it not a fact that when you met Mr. Reuter he had already acquired a number of properties in that section?

A. Yes, I had.

Q. That he had already made contracts for a number of [fol. 97] properties and worked in that section for a considerable length of time?

A. Yes, he told me that he had already signed up some properties.

Q. You testified before that—taking the first one I come to,—here is a contract dated December 27th, 1929, does that refresh your recollection as to anything Mr. Reuter may have said as to how long he had been working on this proposition?

A. I cannot say that it does at this time. I just remember that he told me that he was acquiring other properties in the Pittsburgh territory.

Q. And had already acquired some?

A. I don't know that he said he had,—I think he said he had signed some agreements and options.

Q. As a matter of fact, you now know that he had, previous to the time he met you, acquired various options?

A. Options, yes.

Mr. Hirshfield: That is all.

Redirect examination.

By Mr. Royall:

Q. I am a little at a loss, so I will ask my friend, to be sure, whethert you contest the qualifications of this witness as an expert?

Mr. Hirshfield: I did before and I do yet.

By the Court:

Q. You were born and raised in that country out there?
A. Yes, sir.
Q. Oil and gas have been produced there since you have been there, is that right?
A. Yes.
Q. When did you start getting up these leases?
[fol. 98] A. I have been interested in leases since 22, more or less, with my father.
Q. He was in the oil and gas business?
A. For forty years.
Q. And you traveled about the country with him?
A. Yes.
Q. You know Sam Flannell and Andy Flannell?
A. I know them.
Q. And the relation they bear to the gas producing territory?
A. Yes.
Q. And oil?
A. Yes.
Q. And you have, over that period of years, gone around through the country and taken up leases on various properties or farms?
A. Which I subsequently drilled.
Q. Which you subsequently drilled; did you ever sell any of those leases to Pittsburgh people, to Carnegie or the manufacturers there?
A. No, sir.
Q. Do those leases have a value, as a sort of market through Washington, Greene and Alleghany Counties?
A. As I said before, a dollar or two and in some cases more than that.
Q. In a farm lease next to a producing well, as compared to one in new territory?
A. The acreage would be higher.

Q. And those prices are quoted around the neighborhood, are they not?

A. Exactly so.

Q. Do you keep yourself informed as to the market for oil and gas leases?

A. I do.

Q. Are you yourself competent to pass judgment upon values of leases and of wells?

A. I am.

Q. What value do you ordinarily give to a producing well of a million feet?

A. That is determined by the contract price of the gas. It is possible to determine the total value of flow from a [fol. 99] well, there is a method of doing that, and you are able to estimate the future earnings of the well and arrive at the value of the producing well.

Q. That is well known among gas and oil people?

A. It is known among all engineers—I don't know whether oil and gas.

Q. You have in Pennsylvania a group of men known as oil and gas speculators?

A. We have.

Q. And they trade leases back and forth among themselves and sell them to producing companies?

A. They do.

Q. And the market for those leases depends from time to time and varies, I take it, upon industrial conditions and the amount in production that a company may have at a particular time?

A. Yes.

Q. That is, if the manufacturer has come of its production and wants new leases——

A. If they want new leases, they are willing to buy and pay for those leases.

Q. So is it upon your information that you have gained from your association with your father, and your own experience that you have gained your ideas of the values of these properties?

A. It is through my engineering in addition to the other part.

By Mr. Royall:

Q. You might bring out the additional fact that you have said before that you became active in association with your

father in the business of acquiring and developing gas leases that you also practiced your profession as an engineer?

A. I did.

Q. For a period of about ten years?

A. I did.

[fol. 100] By the Court:

Q. What sort of engineer are you?

A. I have done structural work, road work, building streets, sanitary engineering——

Q. Have you done any geological work?

A. I have studied geology at school.

Q. Have you studied the geology of the oil and gas sands?

A. I have.

By Mr. Royall:

Q. Is it a fact that you were employed from time to time during your engineering career to make surveys of lands for geological purposes such as coal or otherwise in the Alleghanies?

A. I have made geological surveys for coal for the Pittsburgh Coal Compan .

Walter C. Krog, called as a witness by the complainant, testified as follows:

I was formerly employed by Furlaud & Co. with offices at No. 52 Wall Street, New York City, They were bankers engaged in the business of issuing and making publications of securities from time to time.

I am an engineer. I studied at Wisconsin Mining School. Ralph E. Davis was head of the school when I was there; I am a pupil of Ralph E. Davis. I came into the employ of Furland & Co., Inc. about October 15, 1929, and part of my work was to go when I was sent by Mr. Furlaud and Mr. Reuter to make investigations, as an engineer, of properties that they were considering handling.

[fol. 101] Early in 1930, I went to Pittsburgh to investigate and report to them in respect to the properties which were later acquired by the Duquesne Gas Corporation.

I first went there in the middle of December, 1929, with Mr. Schuler, who, I believe, was a financial man and assistant to Mr. Reuter, in the employ of Furlaud & Co., Inc. We had been presented with reports which had previously been made on various properties there, and we then just made a rough and casual survey of these properties. They were the Trafford Coal & Gas Co. and the Campbell Gas & Oil Company properties which were acquired by Duquesne. Ralph E. Davis furnished us with the reports. I next went to Pittsburgh some time in January, 1930, with Mr. Schuler. Mr. Reuter joined us there soon thereafter, and during the month Mr. Halporn joined us; he is one of their financial men.

Mr. Reuter asked me to refer engineers to him who would make a survey for Furlaud & Co. of any properties under option, and I recommended the firm of Ralph E. Davis and arranged for a conference between him and Mr. Reuter. I introduced Mr. Davis to Mr. Reuter. In January, 1930, I was informed by Mr. Reuter that he would employ Ralph E. Davis.

I met a Mr. Robbins who is in the employ of Ralph E. Davis at his Pittsburgh office, and he was delegated by him to take charge of the appraisal work. I attended with him in the field while he was making his examinations of the various properties. A Mr. Henderson and Mr. Jones and Mr. Stevens also assisted him.

While this appraisal work was going on, I was daily in touch with Mr. Robbins and his assistants and getting daily reports.

[fol. 102] The time came when some reports covering five of the properties, and aggregating an appraisal of $1,700,000, including working capital, were rendered by Mr. Davis. This was about the first of February.

Q. I understood you to say that he (Davis) was engaged to report upon all nine of the properties?

A. I don't know what the agreement was with Mr. Davis.

I observed Mr. Davis' staff getting data from the properties.

During this time I often had interviews with Mr. Reuter. I believe he got reports as to the progress of the work from Mr. Davis' office more directly than from me.

Mr. Reuter talked to Mr. Robbins and to me about the progress of the work.

At about February 1st, under Mr. Reuter's instructions, I went to Mr. Robbins, and received the working papers that he had concerning the properties as to which appraisals had not been rendered, and gave them to Mr. Reuter.

Mr. Reuter and Mr. Davis had had arguments. I don't know the extent of it, but Mr. Reuter was extremely angry; talked over the telephone, hung up the 'phone on Mr. Davis and was later called to Mr. Davis' residence, and came back and asked me whether I could refer another engineer to him.

Mr. Reuter said that he felt that Mr. Davis would not give him the values which Mr. Reuter would consider fair values. Appraisals of certain properties had been completed and the wells testified and those figures were given, but there was so much information that had not been completed, that a full value could not be received, and I know he was dissatisfied with the results so far obtained. I don't remember any conversations as to what was arrived [fol. 103] at, whether it would indicate a million dollars or eight hundred thousand dollars, or anything of that sort.

Mr. Reuter called me to suggest another engineer, and asked me to get the working papers away from Mr. Robbins. I got them. I don't think I told Mr. Robbins that his firm was discharged, and I was not instructed to tell him.

I suggested to Mr. Reuter that some one else be employed, such as Brokaw, Garnett, Dixon & Mackay and Ford, Bacon & Davis.

Mr. Reuter told me that one of them was being retained by other parties for work in Pennsylvania, and could not be had, and I don't just remember, but he did not want the other one. I don't remember which was which. I told him that those two firms with Mr. Davis were the three nationally known gas and oil engineers that had been prominent in previous financing, and that I knew of no other nationally known engineer who had been prominent in the Street or in any financing.

He then asked me to suggest another engineer, and I naturally suggested to him my previous associate, Mr. C. S. Conrad of Mattison, Davey & Winters, who at that time was in Houston, Texas, and Mr. Reuter asked me to call him long distance that night, which I did. He came immediately to Pittsburgh and I introduced him to Mr.

Reuter, and evidently they came to an agreement, for Mr. Conrad was retained to finish the work.

I went with Mr. Conrad day by day in the field, and gave him all the assistance I could. Mr. Conrad had no staff then, besides himself. I don't know whether Mr. Conrad had ever acted as an appraiser or engineer in the Alleghany field. I did not ask him. I knew him well, but I had not [fol. 104] known him all my life or all of his. He had been the chief engineer for Mattison, Davey & Winters for several years and, I would say, had done work in the mid-continent field, chiefly.

In the course of two or three weeks during the latter part of February, he produced the appraisal of $5,100,000 for the four other properties. I worked with him while he was making up his appraisal. In some instances he used the Davis material.

There were continuous arguments as to the values being arrived at. I knew there were talks and argumeuts about the speed. I cannot definitely say that I know more, but Reuter was constantly after all the value which we could give him within engineering principles.

I became Vice-President of the Duquesne Gas Corporation before the closing on April 9th. As I recall, I was told by Mr. Halporn of this fact after I became Vice-President. I executed all of the $4,000,000 bonds and $1,000,000 notes as Vice-President on April 7th. Mr. Halporn informed me that we were going to sign the bonds. I had never done anything like that and I was a little reticent about doing it, but I was assured that it was perfectly all right and legal. Mr. Halporn signed as Secretary. We signed the bonds at a signature company, 25 bonds at one time. I did not know anything about corporate proceedings. As far as I can recall, it was the thing that I was asked to do, as vice-president. I signed the notes. I suppose there were a million dollars notes.

I was instructed by Mr. Furlaud and Mr. Reuter to attend at the Central Hanover Bank & Trust Company on the morning of April 9th.

On April 9th, there were present at the closing Mr. Furlaud, Mr. Reuter, Mr. Halporn, myself and a vice-president [fol. 105] of the Central Hanover Bank & Trust Company, Mr. Osborne, and Mr. Duke, who is one of the law firm of Chapman & Cutler, legal advisers. There may have been

others. There were bonds and notes in the cage which looked like the bonds and notes I had seen the day before.

Several papers were placed before me to sign. I started to read them over; Mr. Duke informed me that it was all a matter of form; that it was all right to go and sign anything they placed there and I did so, without reading the papers.

After these papers were signed, we were moving around freely in the room. Mr. Halporn was in the cage, and there was a queue of runners coming from the elevator to the cage with checks or amounts to take up the bonds and notes subscribed and after it was given them they left. The queue in the elevator consisted of about fifteen to twenty men at a time.

The closing lasted from the morning until the middle of the afternoon, up to about three o'clock, I imagine.

Cross-examination.

By Mr. Hirshfield:

I worked with the man from Mattison, Davey & Winters to a great extent, and except that he was the man in charge, and I was working subject to his approval, this report of Mattison, Davey & Winters was as much my work as the work of the man who signed it. I did the work that he asked me to do only. I did not discuss questions of value with Mr. Conrad.

Q. First, who is Mr. Furlaud?

A. Mr. Furlaud——

Q. In connection with this matter. I am not asking for his family history or anything of that kind.

A. What do you mean?

[fol. 106] Q. What relation did he have with Furlaud & Company?

A. He was just a member of the firm of Furlaud & Company.

Q. You had very much to do with him in this deal?

A. Very little to do with him.

Q. Did you see him practically every day in the office?

A. Not for any talk in the office.

Q. Who is Mr. Reuter?

A. Mr. Reuter was another member of Furlaud & Company organization.

Q. You understand, of course, that Furlaud & Company is a corporation?

A. A corporation, yes.

Q. Then may I amend your answer to the extent of saying that Mr. Furlaud was an officer of the corporation and Mr. Reuter was an officer of the corporation?

A. I believe that is so, yes.

Q. Who is Mr. Halporn?

A. To my knowledge, he was an employee of the corporation.

Q. Who was Mr. Schuller?

A. Also an employee of the corporation.

Q. And I understand you were an employee of the corporation?

A. Correct.

Q. At this closing, you said that Mr. Duke was present; who is Mr. Duke?

A. Mr. Duke is a member of the organization of Chapman & Cutler.

Q. And they are employed by Furlaud & Company?

A. Right.

Q. So that everybody at this closing was an employee or officer of Furlaud & Company?

A. With the exception of the bankers.

I have no knowledge whether the checks given to the queue of runners were checks made payable to the Central Hanover Bank & Trust Company or to Furlaud & Company. I did not see them. I saw notes and bonds handed out. I could not distinguish the notes from the bonds.

[fol. 107] Eugene P. Brady, called as a witness by the complainant, testified as follows:

I was formerly employed by Furlaud & Company. I was a member of the sales organization, and in charge of the Middle Western Distribution. My particular duties were to obtain commitments from other dealers who were members of a distributing group, and I had something to do with organizing the distributing group for the sale of bonds of the Duquesne Gas Corporation.

Plaintiff offered in evidence Plaintiff's Exhibit No. 21.

Plaintiff's Exhibit No. 21 is a distributing group letter emanating from the office of Furlaud & Company, which was

sent to about 500 dealers throughout the country. There were two groups—one known as a distributing group, and the other a banking group. The banking group consisted of about five members, and the distributing group of about thirty. The distributing group consisted of retailers who took the bonds for retail distribution, and were located all over the United States.

Plaintiff offered in evidence Plaintiff's Exhibit No. 22, being an advertisement emanating from the office of Furlaud & Company.

Plaintiff offered in evidence Plaintiff's Exhibit No. 23, being a circular distributed by Furlaud & Company with the distributing group letter which was given to any runner on the Street who came and asked for it. The circular was released for general distribution publicly, and ample sup-
[fol. 108] plies of these circulars were sent to the distributors.

(Objections were made to the introduction of Plaintiff's Exhibits Nos. 21, 22 and 23 on the ground that they were not binding upon the defendant Maxine H. Furlaud personally. Objections overruled, and exceptions taken.)

A previous circular which, however, was not distributed amongst the dealers as far as I know, did not segregate the two appraisals by Ralph E. Davis and Mattison, Davey & Winters. The appraisals were presented as a joint appraisal. These circulars were not distributed among the dealers so far as I know, but were destroyed.

Q. Did Furlaud & Company have anything to do with the issuance of this one million dollar advertisement of Duquesne Gas Corporation (document submitted to the witness)?

A. In an indirect way.

Q. Did they cause this advertisement to be inserted?

A. Indirectly. I should say offhand that Cullen & Drew put the advertisement in.

Q. It is signed here by Furlaud & Company, Inc., and Cullen & Drew.

A. Yes, sir.

Q. As a matter of fact, the whole issue was turned over to Cullen & Drew to manage the distribution of, wasn't it?

A. I understand the note issue was sold to Cullen & Drew.

Q. Cullen & Drew did the distribution of it?
A. Yes.

Mr. Hirshfield: I object to that. The witness has answered, and answered correctly, that the issue was sold to Cullen & Drew, and now Mr. Royall asks him if they had the distribution of it.

[fol. 109] By the Court:

Q. Do you mean to say they bought and sold this issue in this advertisement?
A. Yes; your Honor, they bought that and sold them.

By Mr. Royall:

Q. The issue was publicly shot—you know what I mean by that,—was publicly announced by Furlaud & Company and Cullen & Drew, wasn't it?
A. Yes.

Mr. Royall: I offer this advertisement in evidence.
Mr. Hirshfield: I object to it as not binding on Furlaud personally and on the ground of irrelevancy.
The Court: All right.
Mr. Hirshfield: Exception.

(Marked Plaintiff's Exhibit No. 24.)

Plaintiff's Exhibit No. 25, a circular with reference to the notes, was then offered in evidence. (Objection was made to its introduction in evidence upon the ground that it wasn't binding upon the defendant Maxime H. Furlaud personally. Objection overruled, and exception taken.)

Q. Now, I notice that upon Exhibit 23, the circular as to the bond issue, there is a blank space at the bottom of the third page.
A. Yes.
Q. Is there any custom about doing anything with that blank space?
A. These circulars which are distributed to members of [fol. 110] the group at their request, and are without an imprint in that space——
Q. It contains the imprint, doesn't it, of the banking house of issue and of the distributing house—that may be the distributing house who has that particular circular with that imprint, isn't that the custom?

A. Yes, at first this is printed in blank.

Q. Yes, it is printed in blank, then you print the name of Furlaud & Company, then you put on the name of the San Francisco dealer who was the distributor in one case—I don't care whether you use San Francisco, St. Louis, Chicago, but a dealer——

The Court: I understand, you put the name of some house on.

The Witness: Yes.

Q. With Furlaud's name, then you would print them up that way, is that right?

A. No, that is not exactly right. Furlaud's name would not go on it.

Q. Wouldn't any name go on as the banking house of issue?

A. No.

Q. None of the banking house names of issue would go on the circular?

A. Not to the distributing groups.

Q. This circular was sent to the distributing group, wasn't it?

A. Yes, sir.

My business was to obtain commitments from members of the distributing group, and the objective of my activities was to get a lot of distributors to give commitments.

Q. Was this issue subscribed for?

A. Not fully.

Q. To what extent?

A. That I would not know, but I should say somewhere [fol. 111] in the neighborhood of 75 to 80%.

It was the custom to sell to the distributing group members with the provision that any of the original bonds that were re-sold or picked up in the market should be delivered to them at the original price. This had the effect of retaining the original offered price.

The bonds were traded in on the Curb.

The managers of the syndicate did not have to take in their bonds in order to maintain the market in the market operations following the issue because the bonds were convertible into 80 shares of stock, as I remember, at $15.00 a share, and the stock, as I remember at the time, was quoted

in the neighborhood of $14 or $15 which immediately made a market for the bonds in the neighborhood of, I think, around $109. I am not positive of the exact figure. I have no knowledge as to whether Furlaud & Company, Inc., took a position in the market on the bonds.

I had nothing to do with the organization of the secondary distributing group for the bond issue.

Plaintiff's Exhibit No. 26 was offered in evidence. (Objection made to the introduction of Exhibit 26 on the ground that it is not binding on the defendant Maxime H. Furlaud personally. Objection overruled, and exception taken.)

Cross-examination.

By Mr. Hirshfield:

Every commitment I obtained, and every arrangement or sale I made was an "as, if and when issued" basis.

[fol. 112] HARRY J. STEELE, called as a witness on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

I am Secretary of the Duquesne Gas Corporation; I am now in the employ of the Receiver, and I am familiar with its records and books.

These five bound books are the minute books of the corporation.

The Court: They may be considered in evidence as subject to the right of either party to quote from them as you see fit. Why not put them in evidence? They won't have to be printed in the case of an appeal and either side can read into the record any portion of them that he thinks is material to his case.

Mr. Royall: I do not care to offer them in bulk in evidence, and then be bound by everything that is in them whether material or not.

The Court: As a matter of convenience, I will consider the books of the corporation in evidence for the benefit of both parties.

(Marked Plaintiff's Exhibit No. 27, consisting of five books.)

Plaintiff's Exhibit No. 28 offered in evidence is an original check of the Duquesne Gas Corporation drawn to the order of the Central Hanover Bank & Trust Company in the sum of $3,015,000 under date of April 9th, 1930, to satisfy a loan to Kingston Corporation.

[fol. 113] The records of the Duquesne Gas Corporation show the receipt by it on that day of a check from Furland & Company, in the sum of $3,379,500, and after charging to its account the check marked Exhibit 28, there was left in the account of Duquesne Gas Corporation, the sum of $364,500. There was already $500 in the treasury of the corporation that had been put there on the original issue of the 1,000 shares at fifty cents a share which came to the corporation May 3rd, 1930. So that the corporation had $365,000 in the treasury, together with the deeds to these nine gas properties that were conveyed to it.

The account books do not show that any amounts were received by the Duquesne Gas Corporation from the sale of bonds, notes or stock, except the properties and money aforesaid.

Cross-examination.

By Mr. Hirshfield:

On April 9th, 1930, $3,379,500 was deposited to the credit of Duquesne Gas Corporation at the Central Hanover Bank & Trust Company.

The minute books of the Duquesne Gas Corporation (Exhibit 27, at p. 70) indicate that an offer was made by Furlaud & Company to subscribe to 139,000 additional shares of the common stock of the Duquesne Gas Corporation at 50c a share, or a total price of $69,500 which offer was accepted.

It is conceded that the minutes of the Duquesne Gas Corporation say that.

I do not know who the stockholders of the Duquesne Gas Corporation were at the time that resolution was framed. I had custody of the books. Mr. Parisette is an employee of Furlaud & Company. I don't think he had any relation [fol. 114] with the Duquesne Gas Corporation at the time of the closing on April 9th.

Mr. Steele excused.

THOMAS W. DUKE, called as a witness on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

I am an attorney and counsellor at law, admitted to practice in the State of New York. I am a member of the firm of Chapman, Snider, Duke & Radebaugh, whose correspondent counsel in Chicago is the firm of Chapman & Cutler.

I was counsel for Furlaud & Company, took charge of the legal procedure of the organization of the Duquesne Gas Corporation, and the issuing of its securities, and I was the legal adviser of Furlaud & Company, in connection with the integration of the property and general financial corporate set-up of the Duquesne Gas Corporation. I was the Secretary of the Company, and the author of the minutes in its preliminary stages.

These minutes, consisting of three volumes, are the original minutes that were prepared while I was secretary. I don't think I recorded any meetings, but I was secretary of record. I recognize the handwriting of my associates.

I was familiar with this transaction which was carried on under my supervision as to procedural matters, and my firm also had charge of the examination of the titles to the constituent properties that were to be created into the corporation.

[fol. 115] Q. Those were nine separate purchases, weren't they, as you remember it?

A. There were more than that. There were nine separate purchases; then there were some other properties that had theretofore been acquired by Kingston Corporation. I don't know the particular properties, but the whole thing had gone into the general situation.

Q. Did you have anything to do with any of the properties excepting——

A. These nine are the basis.

The nine properties were the Byers, Trafford, Wynn, Garrison, Nuss, Behm, Wally and Campbell properties.

Our Chicago associates had charge of the examination of the titles. The men in the field were furnished by our associate counsel, Chapman & Cutler, and they were acting under

my general supervision; they also assisted in the preparation of contracts for purchase.

I think I drew one contract, the Wynn contract. My associates took care of and supervised all that work and drew the conveyances, and saw to it that the conveyances were executed by the sellers, and that the conveyances and the necessary accompanying documents had been lodged with several conveniently located banks in and about Pittsburgh in escrow, under an arrangement that the escrow depository or local bank was directed and authorized to deliver the deeds over to one or more of several named individuals after drafts drawn by them on designated New York banks for specified amounts have been honored.

These individuals were either members of my staff, or Chapman & Cutler's staff, down there in the field, and one was a member of the Furlaud organization, Mr. Schuller. [fol. 116] Mr. Schuller was not used. He was on my staff in case of an emergency, in case we needed him.

I did not know particularly who were in the selling group. I don't know who were in the Banker's group. So far as I was concerned, the closing would take place when the money would be available to effect closing. They got the money. I knew this was what was known as a public issue.

I arranged the advertisement, or rather I amended it. I possibly passed upon Plaintiff's Exhibit No. 21. It is quite probable that I did not go over these very carefully, because this is a set form which is copied from one by another, and they rarely refer them to counsel. This is a distributing group letter, it is routine work. The Banker's group is generally the keystone of the financial offer. There are three or four men who take the responsibility and this (referring to Plaintiff's Exhibit No. 21) goes to dealers.

There is a subscription blank at the bottom of the exhibit.

Mr. Hirshfield: Your Honor, there is no question in this case that they did not close this thing until they saw fairly well that they could dispose of these bonds, * * * there is no dispute about that.

Mr. Royall: I would like Mr. Duke's testimony on that. Will you read my question?

(Question read.)

Mr. Furlaud and Mr. Reuter were handling the situation, and they informed me that they would be ready to close on April 9th.

They did not tell me how they were acquiring the funds. [fol. 117] I knew how they were acquiring the funds for the actual mechanics of the closing.

Kingston Corporation had been organized some time before. I had no part in its organization.

My escrow sheets showed that in order to clear the nine escrows there would be $2,449,900 required. Mr. Halporn said that $3,015,000 was required, and we thereupon negotiated a loan in that amount. A loan was arranged for the Kingston Corporation at the Central Hanover Bank & Trust Company; it was a one day loan that became effective on the morning of April 9th. With the $3,015,000, Kingston paid the escrows amounting to $2,449,900 on April 9th. Kingston paid it by delivering a certified check to the Equitable Trust Company, in the sum of $804,000 which covered the Henderson Oil & Gas and Nuss escrows, which, in turn, were deposited with the local banks in Pennsylvania. The Nuss escrow was deposited with the City National, and the Henderson was deposited with the Pittsburgh Title & Trust Company. The Equitable Trust Company was the correspondent bank. Kingston delivered another certified check to the order of the Guaranty Trust Company, in the sum of $295,900, which covered the Gallagher and Campbell escrows, both of which were deposited with a bank at Pittsburgh. That was the aggregate amount specified in the escrows of those two-mentioned properties. The balance of $1,350,000 was made up of four drafts on the Central Hanover Bank & Trust Company covering the Degenther or Byers, Trafford Oil & Gas Company, Behm, Garrison and Wally escrows. They were in turn deposited with the First National Bank of Monongalia, Pennsylvania, the Pittsburgh Peoples Trust Company, and the First Bank & Trust Company of Washington, Pennsylvania.

[fol. 118] The $1,350,000, covering the drafts, was applied against the credit established at the Central Hanover Bank & Trust Company for Kingston.

Telegraphic notices were sent by each New York Bank to those correspondent banks notifying them of the acceptance of the drafts. I had received telephone calls from my as-

sociates as soon as they got word that the drafts were paid. Then each man sent me a telegram to the effect that the drafts had been paid and deeds delivered, and were proceeding to record the first and second mortgages, and they in turn were delivered after the deeds were delivered to them.

There were two separate indentures of mortgage—the first mortgage which was closed at $4,000,000 and the second general mortgage synchronized with the first as to its general provisions, but with different trustees, and then there were $1,000,000 bonds authorized, and these bonds, in turn, furnished the collateral for the secured notes. There was a third indenture collateral trust agreement. The first and second mortgages were in the hands of my representatives, and they were recorded at a moment's interval with the deeds.

I waited for confirmation word from my associates to know that the actual properties were in Duquesne Gas Corporation. I got satisfactory confirmation by telegraph and telephone from my associate that the deeds and mortgages had been filed for record.

My notes show that the balance of the loan obtained by Kingston Corporation was paid out by paying $300,000 to Furlaud & Company in accordance with an agreement between Kingston Corporation and Furlaud & Company for expenses that had been advanced by Furlaud & Company, and $250,000 was loaned to Furlaud & Company. I think [fol. 119] above figures were average; that did not particularly concern me in the closing. That was collateral to my problem.

Furlaud & Company negotiated an unsecured day loan in its own name at the Central Hanover Bank & Trust Company for $3,379,500; the $4,000,000 of bonds and $1,000,000 of notes were physically at the closing; Furlaud & Company must have drawn and delivered $3,379,500 on that date to Duquesne Gas Corporation. Duquesne Gas Corporation, pursuant to the plan of reorganization paid to Central Hanover, in repayment of the Kingston loan, the sum of $3,015,000 after Duquesne had acquired its properties.

Until I was satisfied that the whole transaction was ready for completion I did not authorize delivery of the bonds. There was a number of runners there to take up the bonds when released. The entire amount of bonds and notes was

delivered to maybe Kingston and Furland & Co. but as to the distribution from this point I had no part.

The bonds and notes were both convertible into stock. The stock was of one class. Rather, the bonds were made applicable to the purchase of stock the corporation had reserved under contract arrangement. There was no specific law in Pennsylvania as to conversion privileges, so we made the bonds applicable to the purchase, in order to carry out the same intent.

In New York, you can have a convertible bond, a straight convertible bond by just turning it in and getting stock on it. In this case, we accomplished the conversion privilege by making the bonds applicable to the purchase of a specific number of shares, which had exactly the same effect as a [fol. 120] conversion and which made it just a technical compliance with the Pennsylvania law.

We had the authorized stock made available for the purpose. If a bondholder or noteholder saw fit to exercise his conversion privilege, the corporation was in position, at all times, to carry it out.

Q. Did these provisions cover the release of property from the mortgage?

A. Yes, sir.

Q. And the time did come, didn't it, when you were asked to advise the corporation upon the power to effectuate a release from the mortgage of any of the mortgaged companies' leases?

Mr. Hirshfield: I object to that as being immaterial and being outside the issues of the pleadings.

The Court: All right, go ahead.

Mr. Hirshfield: May I except to that?

The Court: Yes.

The Witness: I think Mr. Nuss wrote me, that is quite a while after the closing, I don't remember the date, and since I did not know that this was coming up, I did not bring that information with me, but Mr. Nuss informed me that there were various leases there—originally, I assumed would be drilled, and if not, required certain delayed rentals, and these rentals would impose quite a large burden on the corporation in the absence of building and he wanted to avoid the carrying expense. I went into it very carefully at the time and wrote a letter or helped draft a letter, which

Mr. Nuss sent to the Trustee, notifying him of the action that he intended to take.

[fol. 121] Q. Was this a voluntary release? Was this property to be released without any consideration?

A. I think they were released without consideration.

Q. Do you remember what the properties were, that were released?

A. I don't know. Mr. Nuss told me that some properties were hurting him to carry.

Q. In other words, the properties were a liability instead of an asset, is that it? A. All gas properties are, until they are drilled—not that I am an expert on gas properties, but that is what I have been told.

Q. Did you say the thing was presented to you at the time as a practical matter to deal with?

A. Yes.

The net result of the closing was that $2,449,900 got furnished on that day to the escrow banks, and $365,000 or $364,500 of working capital got furnished to the Duquesne Gas Corporation, and the Duquesne Gas Corporation got deeds of nine properties, and others too. A mortgage securing the $4,000,000 of bonds and a second mortgage securing $1,000,000 notes got recorded, the bonds and notes referred to got issued, and 674,000 shares of stock were issued; 1,000 shares had been issued prior thereto. All of these bonds and all of these notes and stock came to Furlaud & Company or Kingston Corporation. Furlaud & Company, Inc. on that day received at the closing a sum of money the amount of which I do not know. On that day, the aggregate that went into the corporation translated into dollars and cents was $2,449,900 representing the taking up of the escrows, and $364,500 representing the amount of cash left in the Duquesne Gas Corporation.

[fol. 122] In addition to the nine properties that were mentioned before, there were some other properties that were in Kingston or to be taken by Kingston by one of my associates, and he said certain leases were deposited as collateral with John Jones and Val Aitcheson of Washington, and I remember that certain acreage known as the Stybr-Watson leases were acquired from us by Kingston, I believe.

It is a long time ago, and I do not remember the properties. I do not know the basis on which Duquesne Gas Cor-

poration got the Stybr-Watson property; there were some other properties, besides Stybr-Watson, known as Levier, Tucker, White, Wade and Watson properties. I do not know whether my men made an examination of the titles of these properties. The details of the examination of the titles were in each case made on developed leases. It was customary in the gas business not to make an exhaustive examination of undeveloped property. I do not know whether an examination of title was made of this Stybr-Watson property and the other properties.

Cross-examination.

By Mr. Hirshfield:

The check for $3,379,500 paid by Furlaud & Company to Duquesne Gas Corporation, was in payment of the principal amount of the first mortgage bonds at 90, which was $2,430,000, and $1,000,000 of convertible notes at 88 or $880,000, and 139,000 shares of common stock at 50c a share or $69,500.

Q. Now, Mr. Duke, when this property was originally taken over in the early spring of 1930, as I understand it, [fol. 123] these various properties taken over had, in the opinion of the appraisers certain values. Do you know anything at that time of the business conditions in Pittsburgh?

Mr. Royall: I would hardly think this witness was an expert on business conditions; he is just a lawyer.

Mr. Hirshfield: Inasmuch as Mr. Royall has brought up what I consider an utterly irrelevant point about the release, I thought I had the right to show that in the course of the year 1930—and possibly the Court will take judicial notice of the fact—that we were in the midst of what has been commonly known as the depression and the business conditions around Pittsburgh changed very radically.

The Court: I suppose he knows about the conditions there.

The Witness: They were pretty bad.

Mr. Royall: Are you calling this witness to have him tell the Court that there has been a depression in the United States? I will concede that.

Mr. Hirshfield: That is the first concession I have had from you.

Duquesne Gas Corporation was organized on February 21st, 1930, with a capital of 1,000 shares of stock, without par value; the shares wer purchased at 50c a share by Furlaud & Company, or their nominees or dummies..

The capital of the corporation was thereafter increased, and Furlaud & Company subscribed for an additional 139,000 shares at 50c a share. This stock was paid for and issued on April 9th, 1930. Kingston Corporation was a New Jersey corporation, formed some years before.

[fol. 124] On April 7th, 1930, Kingston Corporation and Duquesne Gas Corporation executed an agreement, designated as an agreement of reorganization, which was offered in evidence, and marked Defendant's Exhibit A.

Q. Will you give us the substance of it?

A. Kingston would asquire the properties described in Schedule A annexed to the agreement, these properties being——

Mr. Royall: Has a date been ascribed to this agreement?

The Witness: Yes, April 9th.

Mr. Royall: 1930?

The Witness: Yes. The properties referred to in the schedule were in turn further identified by four separate reports by various engineers, but they were so voluminous that they could not be put into the record. Kingston agreed to acquire these properties and agreed to cause these properties to be transferred and assigned and conveyed to Duquesne Gas Corporation, thus transferring to Duquesne Gas Corporation substantially all of its assets and Kingston agreed to pay all charges and expenses of auditors, counsel, engineers and brokers incurred incident to such acquisition.

Kingston represented that it would be obligated to Central Hanover Bank & Trust Company in the sum of $3,015,000, and in order to effect the reorganization and transfer of assets, Duquesne agreed to pay this obligation upon being assured to their satisfaction that the properties had [fol. 125] been transferred and assigned and conveyed to it. Also upon such assurance to Duquesne, Duquesne agreed to issue to Kingston 535,000 shares of its common stock without par value, together with $1,300,000, principal amount of Duquesne first mortgage 6% convertible gold bonds.

Then Kingston agreed that it would waive any right to subscribe inherent in these shares. Then it is stated that the delivery of the shares and bonds of Duquesne, shall be conclusive evidence of the acceptance by Duquesne of the properties mentioned and shall release Kingston from any and all responsibility with respect thereto, provided that any and all charges which may be made with respect to drilling expenses and of accrued income up to the date of the acquisition of such properties by Duquesne shall be paid by Kingston.

Kingston further agreed that it would pay and reimburse to Duquesne the amount of any and all fees and taxes for organization and of qualification of Duquesne.

The minute book of Kingston Corporation shows that the signing of the said agreement was approved by the Board of Directors.

Q. Do you know, of your own knowledge, on April 9th, 1930, who was the owner of all the issued and outstanding capital stock of Duquesne Gas Corporation? Have you got any stock books here? I think you said you found them.

A. Yes, I have found them. My records show that they were paid for, that is the 139,500 were paid for on that date by Furlaud & Company, Inc. and that the balance of [fol. 126] 535,000 were issued to Kingston Corporation pursuant to the plan of reorganization.

Frank A. Cabeen, Jr. was an employee of the United States Corporation Company of Philadelphia, the firm which performed the corporate services, at our suggestion, for the benefit of Furlaud & Company.

Lee Perot, Jr. was affiliated with the same corporation, and so was B. Rach. That concern furnished incorporators for us, and they were the original three incorporators, furnished to assist us in forming Duquesne Gas Corporation. All were nominees of Furlaud & Company.

F. L. Parisette was an employee of Furlaud & Company and his name was used as the "Street Name" for the Duquesne Gas Corporation stock belonging to Furlaud & Company.

To the best of my knowledge his only interest in the transaction was as representative of Furlaud & Company, Inc.

By Mr. Hirshfield:

Q. On the 9th day of April, Mr. Duke, I am informed that certain loans were negotiated by Furlaud & Company, Inc. with the Chatham & Phenix National Bank in the sum of $700,000, with the Hibernia Trust Company in the sum of $300,000 and the Pacific Trust Company in the sum of $500,000, or a total of $1,500,000; do you know anything about those transactions or those amounts?

A. I could not be absolutely certain about this. I have [fol. 127] some papers that indicate loans like that.

Q Will you look at your papers and see if they refresh your recollection and tell us what you know about that?

A. I just had a carbon, I think, of a letter, giving the collateral security to them—I do not have the original and I could not testify with any degree of certainty, but I have pencil notes that Furlaud & Company was to receive $700,000 from the Chatham & Phenix National Bank, $500,000 from the Pacific Trust Company and I recollect a certain amount from the Hibernia, but I haven't any figures on that because it did not specifically concern me.

Q. I can show that from somebody else, so I won't bother you with that—only one thing more. No bond and no note was released by Duquesne Gas Corporation to Furlaud & Company or to Kingston Corporation, as I understand you to testify until you had been completely satisfied that these bonds were completely and validly issued by Duquesne Gas Corporation in accordance with the plan of the reorganization which you had drawn up?

A. Yes. May I amplify that?

The Court: Yes.

The Witness: You said they were not released until they were validly issued. They were not released until I was certain first, that every property that was contracted for had come in and its title was cleared. Second, that Duquesne in its treasury in cash $365,000 to make it responsive to the circular, and at that point, I released the bonds.

[fol. 128] By the Court:

Q. Assuming them valid?

A. Yes, sir.

Mr. Hirshfield: That is all.

Redirect examination.

By Mr. Royall:

Q. Did you complete your explanation about your answer to the last question?

The Court: He qualified it and said that he assumed it was valid at that time.

Q. There was read in the question, according to the plan of reorganization, and I call your attention to that, and I will ask you do you mean to say that you waited to be satisfied about anything else than that the properties had been conveyed and the mortgage recorded and the $365,000 put in the treasury, and that is all you wanted before you rang the bell to proceed, is that right?

A. Yes.

Q. You did not know whether Furlaud & Company got the money to provide for those two things just mentioned, namely, the release of the escrows to get the title and for the $365,000 in the treasury, you don't know whether they got that money wholly from bond subscriptions taken up on that day or partly from some loans they made or may have made that day or where the money exactly came from, is that right?

A. No, so far as I was concerned, that money was a day loan from the Central Hanover Bank & Trust Company and placed under my supervision to clear the transaction. That was a loan. How that loan was repaid I am not in position to say.

[fol. 129] Q. You don't know?

A. No, sir.

By Mr. Hirshfield:

Q. That was the money that was used?

A. Yes.

By Mr. Royall:

Q. Your chief function and your great concern was to have your own counsel, which was referred to in this bond issue, justified?

A. Absolutely.

Q. And that opinion, in order to be justified, had to have lying under it the accomplished fact of the filing of the

mortgage for record and the payment of the $365,000 cash into the treasury of the corporation?

A. And the acquisition of the properties which the engineers had appraised. It had to be those specific properties.

Q. Those specific properties, and the subjection of those properties to the mortgage,—I intended to include that.

A. Yes.

Q. That was your concern?

A. Yes.

Q. And you were concerned about that, because that was a public issue?

A. Yes.

Q. And in which the opinion of your firm was referred to, as counsel?

A. I stated that all matters were under our supervision.

Randolph C. Coleman, one of the original subscribers to the stock of the Duquesne Gas Corporation, and a director and officer of that corporation, was an employee of my office, and could be called a nominee or dummy for Furland & Company, Inc.

McLane Tilton, a director and officer of the Duquesne Gas Corporation, acted in the same capacity.

[fol. 130] Redirect examination.

By Mr. Royall:

The circular issued stated that there was $365,000 in the treasury of the Duquesne Gas Corporation, and that is what I had to have, that exact amount.

I only made an exhaustive examination of titles of properties which were actually being operated. The detailed examination was more general as to unoperated properties.

Herbert J. Osborne, called as a witness on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

I am Assistant Vice-President of the Central Hanover Bank & Trust Company.

On April 9th, 1930, we made a loan of $3,337,500 to Furlaud & Company, secured by the bonds and the notes of Duquesne Gas Corporation.

We made an unsecured loan of $3,015,000 to Kingston Corporation, and that was cleared off at the same time. The loans to Kingston Corporation and to Furlaud & Company were made at the request of Mr. Furlaud. The loan of $3,015,000 to Kingston was paid off with the check of the Duquesne Gas Corporation. The Furlaud & Company loan was paid off by a lot of certified checks of various banking houses drawn on New York banks.

At the closing, there was a delivery of bonds to a procession of runners against certified checks. I do not know the extent of delivery of bonds. I know that a good part of our collateral was delivered out when we got the certified [fol. 131] checks; certified checks were given to Furlaud & Company who endorsed them to our bank.

Kingston Corporation opened a bank account on April 5th, before they applied for the loan. There was a deposit of $29,500 on that day, and $3,015,000 thereafter. The transcript records payment on April 9th of $804,000, $295,900, $265,100, $300,000 and $1,350,000, so that the whole $3,015,000 was paid out on the same day.

The Bank always had a string on the money.

Edward S. Travers, called as a witness on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

I am head of the Incorporators' Department of the Manufacturers Trust Company, which became the Transfer Agent of the Duquesne Gas Corporation on April 26th, 1930.

Our original entry was made from a certificate made by Robert Halporn dated the 24th day of May, as of the close of business on May 15th, 1930, and it listed the stockholders of Duquesne Gas Corporation, certificates, and number of shares of each certificate. This showed that the certificates, aggregating 675,000 shares of the common stock of Duquesne Gas Corporation, were all registered in the name

of F. L. Parisette. On a certificate for 3,000 shares of the original 675,000 shares, the following stamp appeared:

"This certificate cannot be sold, transferred or delivered prior to March 26th, 1931, without the written consent of Furlaud & Co., Inc."

[fol. 132] Q. What are the certificates that it does appear on, subsequent certificates?

A. Subsequent certificates.

Q. We will have to go into those and see all about it. Were these subsequent certificates also issued in the name of Parisette or in somebody else's name?

A. They were originally issued in the name of Parisette and they were split up, as we call it, into smaller denominations, which were subsequently issued from the name of Parisette into other names, then back to Parisette in some cases. In other words, that was an account which varied greatly from day to day.

Q. See if I understand this. The certificates aggregating 675,000 shares were later split up into a large group of certificates representing smaller numbers of shares each and then this stamp was placed upon them in that form, that is the way it was?

A. Yes.

By Mr. Hirshfield:

Q. That was after May 15th?

A. Yes.

From May 15th, 1930 to October 1st, 1930, there were issued 4,300 one-hundred-share certificates and 4,000 less than one-hundred-share certificates.

Roger A. McShea, Jr., called as a witness on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

I am an accountant employed by the Pennsylvania Public Service Commission, and I was sent to the office of Furlaud & Company, New York City, for the purpose of getting data

[fol. 133] and reporting to the Commission the facts concerning the issuance of the securities of Duquesne Gas Corporation. I conducted an examination at the office of Furlaud & Company from July 20, 1931, to July 24, 1931. I have some notes in condensed form concerning the operation of the bond syndicate after the issuance and the marketing of the bonds which I took from the books of Furlaud & Company, Furlaud Reuter & Company, Kingston Corporation and Byron Corporation.

Q. Do those records show the acquisition by Furlaud & Company, Inc. of $4,000,000 of face amount in bonds?

A. Yes, sir.

Mr. Hirshfield: May I object to this question on the ground that the witness is only speaking from his notes.

Mr. Royall: I call upon you then to produce the books of Furlaud, Reuter & Company, Inc. Of course, this is going to take a great deal of time, but we will have to do that. We have subpœnaed the books.

The Court: Perhaps by consulting your working papers, you can pick out the spots where these are located.

Mr. Hirshfield: You may testify from the books here so that Mr. Royall may offer these books in evidence if he cares to.

Mr. Royall: I offer the books of Furlaud, Reuter & Company in evidence, all their account books, if that is what you want. I don't know what is in them, but I will offer them.

Mr. Hirshfield: Now, your Honor, may I interpose this [fol. 134] objection? Mr. Royall, in his various interlocutory motions, a number of times said that his theory of this case is the exact amount of profit made by these various people, was not a matter for this court, but was a matter for subsequent accounting. Remember, this complaint is for an accounting. At the very early start of this case, I made a motion to compel a more definite and certain statement of facts in the complaint, but I was met with the opposition and Judge Caffey denied my motion upon the ground that it was stated by the attorneys for the plaintiff that all that they were trying to show was that there was something due and that an accounting should be had and that the amount that they asked for, specifically the exact amount that we were supposed to be accountable for, and how it was taken, and they succeeded in evading that and

preventing our motion to dismiss on the complaint by the statement that all they were looking for was an accounting, so I submit, on that theory all this testimony is entirely irrelevant at this point.

The Court: I don't know what the purpose of it is.

Mr. Royall: This is a suit for an accounting. If we can prove here and now, and I think we can, what the trustees received—what these fiduciaries received, we have proved what the corporation got out of it, which we have to prove out of their own books, of course, what they received and your Honor could, if your Honor sees fit, make an inter- [fol. 135] locutory decree and appoint a Master, and all these books would be brought before the Master, involving great expense and delay in this Receivership, but I believe, your Honor, an hour or two more of examination and we will have all the facts and features before you, gotten right out of their own books.

He complains that we did not tell him the exact amounts they were accountable for. The Trustee knows what money was received. We don't know. We have to get it out of the records.

The Court: You want to show the profits they made out of this transaction?

Mr. Royall: We want to show the moneys they received, the amount they received out of the bond issue, and we claim they are accountable to us for that. That is our whole case.

The Court: What do you want to show now?

Mr. Royall: What money Furland & Company received from those bonds, notes and stock.

The Court: All right.

Mr. Hirshfield: Exception.

(Marked Plaintiff's Exhibits 29 and 30.)

Mr. Hirshfield: May I again renew my objection to this testimony? I did not have before me these documents this morning. Here is a brief which was submitted by my learned adversary on the original motion to make more [fol. 136] definite certain matters and his brief says that manifestly there is but one cause of action and manifestly this is a suit for an accounting, and so on.

Subsequently, there was a motion made by the plaintiff for leave to propound certain interrogatories which was

argued before Judge Woolsey. There was no objection to the first three interrogatories and Judge Woolsey allowed them. Now, my point of objection at this time is that we are not prepared, and do not expect to be prepared on this trial, because there was no notice to us to go into any testimony at all as to any expenses or any offset as against the testimony of what these proceeds were.

The Court: Until I know that there was something received by the defendants in this transaction, I have no basis of finding that there was fraud against them—I will allow it at this time.

Mr. Hirshfield: I will take an exception to your Honor's ruling and I will renew my motion later on.

From the working papers in my hand, I am prepared to testify as to what Furlaud & Company received from the sale of Duquesne Gas Corporation bonds. The books show the receipt by Furlaud & Company of $4,000,000 of Duquesne Bonds, and also various purchases of Duquesne bonds by Furlaud & Company. Additional purchases, over and above the $4,000,000 bonds, amounted to $1,194,000 par value, for which was paid on account of the purchase price, commissions, interest and so on, $1,309,662.76. The books [fol. 137] show that all of these bonds were sold for the aggregate amount of $4,941,333.80. The books show the receipt of $1,000,000 of notes. There were miscellaneous purchases of notes totalling $6,000, par value at a cost of $5,448.87. Furlaud & Company sold the $1,000,000 par value notes, and the $6,000 par value notes which they purchased shortly thereafter, for $886,546.56.

I also examined the books of the Byron and Kingston Corporation, as well as Furlaud & Company, but I did not examine the books of Chaucer Corporation. I was told that these books were in California.

Q. Were you able to analyze from the books of the Kingston Corporation, Byron Corporation and Furlaud & Company, any transactions relating to the disposal of the capital stock or any part of the capital stock of the Duquesne Gas Corporation?

A. Yes, sir.

Q. Will you tell us what your examination and analysis discloses as to that?

A. This is in connection now with the Byron Corporation. On June 4, 1930, the Byron Corporation sold 12,500 shares of Duquesne common stock to John J. Bergen at $10 a share and received on the same date cash in the amount of $125,000.

Q. All right, continue.

A. On June 5th, 17,500 shares were sold at the same price, and cash was received of $175,000.

On June 6th there was 12,500 sold at the same price and on that day there was received $125,000 in cash, making a total number of shares sold of 42,500, for which was received $425,000.

Q. All from Bergen?

A. All from Bergen; yes, sir.

[fol. 138] Q. Now, then, were you able to construct from any data in the books of Byron Corporation, Furlaud & Company and Kingston, entries relating to this stock, from which you could testify to any other transactions relating to the sale of the stock?

A. Of course, the sale of this stock to Mr. Bergen was covered by a joint contract by the Byron and Chaucer Corporations and this contract provided that Mr. Bergen would purchase this stock in various blocks at different prices according to the block, and as he purchased the stock, one-half should be sold by Byron and one-half should be sold by Chaucer.

Mr. Royall: I call on the other side to produce the agreement between Byron and Chaucer Corporation with Bergen, as described here by this witness.

(Document handed to counsel.)

Q. I show you a paper produced by the other side and ask you if that is the contract that you have just referred to?

A. I believe this to be the contract.

Mr. Royall: I offer it in evidence.

(Marked Plaintiff's Exhibit No. 31.)

Mr. Hirshfield: Your Honor, of course that is subject to the same objection, as well as all this line testified to by Mr. McShea.

The Court: All right.

Mr. Royall: The contract is rather long and the other side will correct me if I misstate the substance of it, with- [fol. 139] out the details. The substance of it is, it is a joint contract between one John J. Bergen and the Chaucer Corporation in the form of a letter to the Chaucer Corporation and Byron Corporation, a joint letter dated May 29th, 1930, signed Chaucer Corporation by Carl S. Reuter, President, and Byron Corporation by James P. Cleaver, President. It covers the sale of or grants the right to Bergen to purchase shares of stock of Duquesne Gas Corporation to the extent of 100,000 shares at $10 per share, or any part of these 100,000 shares at $10 a share and all or any part of an additional 150,000 shares at $12 a share, the contract performed equally by Byron and Chaucer Corporation, and appended to it is the following guaranty of performance:

Furlaud & Company, Inc. being greatly interested in the performance of the foregoing agreement and being desirous that John J. Bergen shall enter into this agreement hereby guarantees performance by the Chaucer Corporation and Byron Corporation under the terms and provisions of the foregoing contract.

Q. Now, in answer to my last question as to whether or not you were able to trace out of the books of Byron, Kingston and Furlaud any transactions by the Chaucer Corporation in respect of the sale by it of any of the Duquesne stock, and in answer to that, you referred to this contract, when I interrupted you to put the contract in evidence. Now, will you continue your answer?

A. Of course, when I was there at the time, not having [fol. 140] the Chaucer books available, I asked Mr. Parisette what the holdings of each of Furlaud & Company and Byron Corporation and the Chaucer Corporation were in the stock of the Duquesne Gas Corporation. He jotted a memorandum which I have now and he stated that Furlaud, Reuter & Company had 2,240 shares; Byron Corporation 174,200 shares and Chaucer Corporation 163,600 shares.

Incidentally, as far as Furlaud is concerned I think Mr. Parisette made a mistake in jotting this amount down, because I found out later that 2,240 shares was what was in

the box at the time I was there, and not what was charged in the investment account, but in the case of the Byron Corporation, I was able to verify the fact that Byron's investment covering the stock of Duquesne Corporation amounted to 174,200 shares.

Now, then, by duplicating the sales of the Byron Corporation to Mr. Bergen and taking the sales Byron made and assuming that Chaucer's sale would have been the same, and then taking into consideration also the sales of Byron Corporation to Furlaud, Reuter & Company at various prices, I was able to determine from the Furlaud, Reuter books that Furlaud purchased from Chaucer 10,600 more shares from them than they did from Byron, and the difference between the Byron investment account in that stock and the Chaucer investment account as given me by Mr. Parisette, that seems to check, that is the difference in the two investment accounts was 10,600 shares. That is accounted for by the fact apparently that Chaucer sold 10,600 more shares to Furlaud than Byron did.

Q. Were you able to spell out anything with respect to sales by Chaucer——

[fol. 141] By Mr. Hirshfield:

Q. Just a moment, when you speak of Furlaud, you mean Furlaud & Company, Inc?

A. Yes, that is right, I am speaking of the corporation.

Q. Would you be careful to make that distinction?

A. Yes.

By Mr. Royall:

Q. Were you able to spell out of these analyses the existence of any transaction by Chaucer in the performance of this Bergen agreement, delivery and sale of any Chaucer stock,—of Chaucer's Duquesne stock to Bergen? You testified to the receipt of $425,000 on the Byron books for 42,500 shares and 42,500 on the Byron books; were you able to spell out anything with respect to the sale by Chaucer to Bergen?

A. Of course, I did not see any books of any kind or any records as far as Chaucer were concerned.

Mr. Royall: Have you got the Chaucer records here? Is that young man here who was subpoenaed to produce them, who was secretary of the Chaucer Corporation?

Mr. Hirshfield: They are not in his possession.

Mr. Royall: He swore in the course of the suit that they were in his possession.

Your Honor, the Chaucer Corporation and Byron Corporation made a motion to dismiss the subpœna on the ground that they were not doing business in New York. That motion was based on the affidavit of Coonrod, who was secretary and said that he had the books in his possession. [fol. 142] We have subpoenaed these books and served the subpoena on Mr. Coonrod and Mr. Coonrod swore, I understand—Mr. Coonrod is a member of your office?

Mr. Hirshfield: That is right. He was a dummy officer.

Mr. Royall: Whether dummy or not, he is the secretary and he has to have some representation in the corporation.

We have subpoenaed those books and records, if the Court please, and I submit we should be entitled to see them.

The Court: Let us have him here and hear what he says.

Q. Mr. McShea, either from conversations with Mr. Parisette or other members of his staff——

Mr. Hirshfield: Whose staff?

Q. (Continued.)—Furlaud & Company, Inc. or Maxime H. Furlaud or Carlos Reuter, talks with Mr. Parisette or other members of that office, examining the Bergen contract, examination of the Furlaud books, Byron books, Kingston books, were you able to construct an account of the sale of any other shares to Bergen & Company other than the 425,000 shares that you have testified about?

A. No, sir.

Q. I am not asking from books alone, I am asking from statements made by Mr. Parisette or otherwise?

A. Those 425,000 shares to Bergen, is all I know of except what was apparently sold by Chaucer.

Q. I am asking you about Chaucer. I am asking you if you have got any information in these examinations relat- [fol. 143] ing to the matter of the sale by Chaucer?

A. Of course, I have the contract, but I believe from that, that Chaucer sold the same number of shares to Bergen that Byron did.

Q. Were any statements made to you by Parisette or others to that effect?

A. No, I don't believe so.

Q. Will you refresh your recollection by reading what I show you here?

A. I just don't know what you mean, Mr. Royall.

Q. Have you read this, "85,000 shares sold to Bergen", where did you get that from?

A. From my assumption, in accordance with the contract, that Chaucer also sold 42,500 shares, I worked this up on that assumption, which was based upon the contract.

Q. You assumed that the contract was performed 50-50, as the contract on its face indicated it was intended to be?

A. Yes, sir.

Q. And that upon that assumption, if it was performed 50-50, Chaucer sold another 42,500 shares to Bergen?

A. That is right.

Mr. Hirshfield: I object to that ground of assumption.

Q. I mean that is the best you can testify on that score?

A. Yes.

Kingston Corporation acquired 535,000 shares from the Duquesne Gas Corporation, under the terms of the reorganization agreement. Twenty-five thousand of those shares were transferred to Furlaud, Reuter & Co., Inc., as a dividend in kind on June 4th, 1930. On the same day, there was a dividend in kind declared to Furlaud & Company, Inc., covering $1,300,000 bonds. The Furlaud & Co. books record the receipt of the stock and bonds.

[fol. 144] There are two letters, one written by the Chaucer Corporation and another by the Byron Corporation, both dated May 27, 1930, and both addressed to the Kingston Corporation, New York City, which indicate or explain how options were given to certain individuals carrying with those options the right to acquire the stock of the Duquesne Gas Corporation from the Kingston Corporation at the price of 50 cents a share during 1930.

Q. Will you name the individuals?

A. Shall I read part of the letter?

Q. Yes, if you have a copy of the letter here, read it.

Mr. Hirshfield: Let us have it from the original source, if we can lay our hands on it.

Mr. Royall: Perhaps I can just read it.

"May 27, 1930.

Kingston Corporation,
New York, N. Y.

GENTLEMEN:

We are the owner by assignment of certain options given by you originally to Elsie Reuter and to Carlos Reuter to purchase 55,000 shares and 200,000 shares respectively of the common capital stock of Duquesne Gas Corporation for 50 cents a share, which options are good until January 1, 1931.

We hereby propose to exercise the foregoing options immediately upon condition that you accept from us our two demand notes in the sums of $27,500 and $100,000 respectively, both notes payable with interest at 6% at the [fol. 145] office of the Corporation Trust Company, 7 W. 10th St., Wilmington, Delaware.

We propose to enter immediately into an option agreement with John J. Bergen requiring the deposit by us of the aforesaid stock and by virtue of which Mr. Bergen will obtain an option to purchase the common capital stock of the Duquesne Gas Corporation, and we agree to pay the foregoing notes upon the exercise by Mr. Bergen of his option to purchase the first block of 100,000 shares of the common capital stock of the Duquesne Gas Corporation.

We also desire you to issue to us in the event that our proposal is accepted, one certificate representing 55,000 shares of the common capital stock of Duquesne Gas Corporation to cover the stock originally optioned to Elsie Reuter and certificates representing the balance of 200,000 shares in whatever form you may desire.

Your acceptance of this proposal will give this the force of a contract between us.

Very truly yours, (Signed) Chaucer Corporation, By Carlos Reuter (L. S.) Pres. Accepted: Kingston Corporation, By Robert Halporn, Asst Sec'y."

Mr. Royall: Will you refer me to a similar letter from the Byron Corporation?

(Document handed to counsel.)

Mr. Royall: Here is a letter dated May 27th, 1930, the [fol. 146] same date as that addressed to Kingston Corporation, New York, New York:

"We are the owner by assignment of an option given by you originally to Maxime H. Furlaud to purchase 255,000 shares of the common capital stock of the Duquesne Gas Corporation at 50 cents a share, which option is good until January 1, 1931.

We hereby propose to exercise this option immediately upon condition that you accept from us our demand note in the sum of $127,500 payable with interest at 6% at the office of the Corporation Trust Company, 7 West 10th Street, Wilmington, Delaware.

We propose to enter immediately into an option agreement with John J. Bergen, by virtue of which Mr. Bergen will obtain an option to purchase some of the common capital stock of Duquesne Gas Corporation and we agree to pay off the foregoing note upon the exercise by Mr. Bergen of his option to purchase the first block of 100,000 shares of the common capital stock of Duquesne Gas Corpporation.

Your acceptance of this proposal will give this the force of a contract between us.

Very truly yours, Byron Corporation By James P. Cleaver, president. Accepted: Kingston Corporation, by Robert Halporn, Assistant Secretary."

James P. Cleaver was President of Byron Corporation and was not an employee of Furlaud & Company, Inc.

[fol. 147] My notes indicate that the records of Kingston Corporation show they received the notes from Byron Corporation and Chaucer Corporation and that on December 2, 1930 Byron Corporation paid interest of $3,995 and $127,500 on account of principal of the note. My notes indicate that there is another entry on the same date in the same total amount with the name Chaucer with a question mark after it.

In addition to the dividend in kind of Kingston Corporation, there was a cash dividend declared, payable as follows: $5,500 to Robert Halporn on one share of stock; $5,500 to M. H. Furlaud on one share of stock, and $264,000 to Furlaud & Company, Inc. on 48 shares of stock, making a total of $275,000.

Q. Which is the sum total of those two payments we just traced in there, isn't it?

A. Well, it is about $12,000 more; do you want the exact amount?

Q. Yes, give us the exact amount.

A. Those two cash receipts amounted to $262,980 in total and the cash dividend amounted to $275,000.

Q. The amount of this cash dividend was the amount of these recorded payments from Byron Corporation and Chaucer Corporation (with a question mark) plus what amount of money—you mentioned the amount of money plus $12,000?

A. I can give you the exact amount.

Q. Just make the computation.

A. That amount is $12,020.00.

My records do not show who the directors, stockholders or officers of the Byron Corporation and Chaucer Corporation were. It is stipulated that Elsie Reuter is the wife [fol. 148] of Carlos Reuter, and Eleanor Furlaud is the wife of Maxime H. Furlaud.

Mr. Hirshfield: I want to renew my motion to strike out the testimony of this witness.

The Court: Motion denied.

Mr. Hirshfield: Exception.

Eugene P. Brady, recalled by the complainant, testified:

By Mr. Royall:

I stated yesterday that to my knowledge, at the time of the issue, there were no market operations, as you call it, as of April 9th, or so. However, subsequently there was continued buying and selling from a period of about June to October, 1930, where different bonds were bought on the market, and sold through the secondary distributing group. I have no idea as to the number of bonds on hand at the start of the operation. I should say there were in the neighborhood of $2,000,000 sold during that operation.

At the time of the organization of the secondary group, I guess there were some $800,000 in bonds left, and there were acquisitions in these market operations. The second-

ary distributing group was organized to float the balance.

These bonds were admitted to trading on the curb, and were traded on the curb during that period. The plan of the distributing group was that the distributors were to be allowed to take the bonds down, the bonds which they sub-
[fol. 149] scribed for, at the then market, less two points on sales up to 15 bonds, three points on sales from 15 to 25, and 3½ points on sales over 50 bonds. These figures were off the day's market prices.

In the secondary operation, the price started, as far as I can figure, at 88 and as of September 30th, a high of 95¼ was reached. On October 30th, the market had receded to 84½, at which time I think the operation ended.

Paul M. Coonrod, called as a witnes on behalf of the plaintiff, testified as follows:

Direct examination.

By Mr. Royall:

The copy of the subpoena shown to me was served upon me. It requires production of the stock ledger, ledger, minute book, letters, contracts and other documents of Chaucer Corporation. I have produced only the minute book of the Chaucer Corporation for the trial.

The information as to one or two isolated transactions referred to in my affidavit of April 12th, 1932, came from the minute book. The isolated transactions involved a transaction with John J. Bergen in May, 1930, relating to the exercise of an option by the Chaucer Corporation to purchase 255,000 shares of the Duquesne stock, and to the signing of a contract between Chaucer Corporation and John J. Bergen to sell him certain securities, all of which is embodied in certain resolutions appearing in the minute book of Chaucer Corporation.

Tillie Pollack mentioned as a director, is a stenographer in the office of Eppstein & Hirshfield, by which firm I am also employed.

[fol. 150] I believe that Carlos Reuter was President of the corporation at that time

I was Secretary of the corporation.

Q. There is recorded in this minute a resolution that "This corporation exercises the options to purchase 255,000 shares of the capital stock of Duquesne Gas Corporation from the Kingston Corporation acquired by it from the Virgil Corporation upon condition that the Kingston Corporation agrees to accept from this corporation demand notes of this corporation for the consideration to be paid for the said stock."

A further resolution is recorded:

"Resolved that the Secretary of this corporation be and he is hereby directed to do all things that may be essential to effectuate the exercise of said option."

May I pause for a moment to ask if the secretary there referred to was yourself; was it?

A. Yes.

Q. The president presented a resolution in which it was proposed that the corporation enter into a contract with J. J. Bergen, which contract is as follows—may I pause to ask if the president refers to Carlos Reuter?

A. I believe he was president at that time.

Q. Then there is attached a copy of the form of contract. The contract between the Byron Corporation and the Chaucer Corporation which has been put in evidence here as Plaintiff's Exhibit 31; I will show you Exhibit 31 if you have any doubt about that, so that you can see it is the same contract that is in your minutes (document handed to the witness). Don't make any long comparison, just [fol. 151] enough to satisfy your conscience that it is the same. I will say that this contract was produced from your files.

A. That is right.

Q. The resolution in the minutes refers to contract, Exhibit 31?

A. That is right, yes.

Q. I want to call your attention to this resolution that I read:

"Resolved that this corporation exercise the option to purchase 255,000 shares of the capital stock of Duquesne Gas Corporation from the Kingston Corporation acquired by it from the Virgil Corporation upon condition that the Kingston Corporation agrees to accept from this corpora-

tion demand notes of this corporation for the consideration to be paid for said stock."

Will you translate the meaning of that resolution to me?

A. I know nothing about the resolutions shown to me, except what I see here. I was a dummy director, and I did only what I was told to do by Mr. Eppstein or Mr. Hirshfield. I know nothing about the matter, other than what you will find in the book.

I know practically nothing about the Virgil Corpporation referred to, except that I believe it was organized in our office, but I had nothing to do with it. I do not know whether I am an officer of the Virgil Corporation. I am a dummy director in quite a few corporations.

Another transaction was the offer on May 16, 1930, by Elsie Reuter to exchange 1,000 shares of the common stock of Furland & Company, Inc. for 10,000 of the capital stock of the Chaucer Corporation, each in the par value of $100. [fol. 152] The offer was accepted by Marion Goodman for Chaucer Corporation.

Marion Goodman whose name is mentioned in the minute book is a secretary in the office of Eppstein & Hirshfield. She was secretary of the Chaucer Corporation at the time. As far as I know the Chaucer Corporation is still in existence. I believe I am still secretary of it now.

I do not know whether Bergen ever bought any of the shares which are the subject of the contract shown to me. I do not know who the stockholders of the Chaucer Corporation are; I may have known at one time who the stockholders were, but I don't remember anything about it now. I have no idea for whose purpose the corporation was brought into existence. I merely acted as a dummy throughout the entire transaction.

Carlos Reuter actually attended the meetings recorded here; the meetings were actually held as set forth in the minutes and were attended by the directors. Those present besides Mr. Reuter and myself were Tillie Pollack and Marion Goodman, both employees in Eppstein & Hirshfield's office.

I have no other information about the matter. There were no stockholders' meetings of Chaucer Corporation called, except the original incorporators' meeting; the original incorporators were Marion Goodman, Mildred S.

Reisman and Tillie Pollack, all of whom are employees in our office.

I have heard of James P. Cleaver. I don't know much about him; I merely saw him in the office, and that is all that I know about him. He was formerly in some branch of the stock business.

[fol. 153] Lyon F. Terry, called as a witness on behalf of the complainant, testified as follows:

Direct examination.

By Mr. Royall:

I am a member of the organization of Ralph E. Davis, at the New York office. Some time in March, 1930, I went to the office of Furlaud & Company, and saw Mr. Reuter and Mr. Furlaud in connection with the circular they were then issuing. I told them that I had a telegram from Mr. Davis in which he objected to the manner of the use of his name and requested that they separate the values of the property named in the circular, because it created the impression that we subscribed to the total value at $7,000,000. The circular originally spoke of a joint appraisal, and we wanted to separate the properties that were appraised by us and the properties appraised by others.

By the Court:

Q. Did they say anything why they so represented it as being worth seven million dollars and using your name jointly with someone else's?

A. That was their affair and we had nothing to do with it.

Q. I asked whether they said anything to you as to why they had done that.

A. I do not recall, sir, whether they said anything in that regard or not.

Cross-examination.

By Mr. Hirshfield:

Q. Mr. Terry, as I understand it, subsequent to your visit to the office of Furlaud & Company, Inc., and in your con-

[fol. 154] versation with Mr. Reuter, they amended the circular so as to meet with your approval?

A. They did, sir.

Q. Just to refresh your recollection, I show you a paper which I think has your signature on it so that you can be quite certain and the court will understand that your objections were met.

A. Yes, sir; I recognize the signature to that.

Q. That is your signature?

A. Yes, sir.

Mr. Hirshfield: That is all.

Cyrus C. Robbins, called as a witness on behalf of the complainant, testified as follows:

Direct examination.

By Mr. Royall:

I am an engineer, and I was associated with Ralph E. Davis, until February 1st of this year. I was associated with the Pittsburgh office of the organization.

Q. What, if anything, did you have to do with making appraisals of properties that became constituent with the properties of the Duquesne Gas Corporation?

A. I completed appraisals on five of the properties and made field examinations of four of the properties.

I was here when Mr. Krog testified.

About February 1st, 1930, after I had rendered five appraisals, Krog came to me and asked for my working papers as to the other four properties on which I had not rendered appraisals. I had three assistants with me in the field doing the work there, and we had gathered data respecting other properties on which appraisals had not been rendered.

[fol. 155] At various times, Mr. Reuter would come into our office and asked me what values we were getting on these properties; he came in from day to day, and while our work was in preliminary form, I gave him such information as I got from those preliminary appraisal schedules.

Q. Did you give him anything to indicate any values in dollars and cents, what your appraisals would work towards with respect to the Nuss property and what were the names of the four properties—the names got mixed up—that you had not reported on.

A. Nuss, Behm, Wally and Byers and there was at that time property on which I had not collected data on, Garrison.

Q. Now, as to those four first mentioned which you indicated to Mr. Reuter in a preliminary way, what your work was leading to in dollars and cents, what did that indicate?

A. So far as the operated properties were concerned, I think it indicated between $800,000 and $1,000,000. That did not, however, include the Behm property, as I had not worked any preliminary schedules on that as yet.

Mr. Hirshfield: Your Honor, I object to this line of testimony on the same grounds as before.

The Court: Yes.

Mr. Hirshfield: Exception.

OFFERS IN EVIDENCE

Counsel for complainant thereupon read into the record the following facts:

"Certificate of Incorporation of Furlaud & Company, Inc., filed in New York County July 18th, 1928.

[fol. 156] Certificate of Change of Name to Furlaud, Reuter & Company, Inc., filed August 1, 1930.

Certificate of Change of Name to Winchelsea Holding Corporation filed October 10, 1931. Certificate of dissolution was filed October 27, 1931."

Thereupon counsel for the complainants read into the record the following statements appearing in the answers to certain interrogatories propounded to the defendants.

The stockholders of Byron Corporation from February 1st, 1930, to date, and the number of shares held by each one are:

Eleanor M. Furlaud, from May 10, 1930, 10,000 shares.
Kipling Corporation, from May 15, 1930, 30,000 shares.

The following were the directors of the Byron Corporation from February 1st 1930:

Paul M. Coonrod,
Tillie Pollack,
James P. Cleaver.

The following is a list of each and every officer of the defendant Byron Corporation, from February 1, 1930:

President—James P. Cleaver,
Secretary—Paul M. Coonrod,
Treasurer—Paul M. Coonrod.

In the answers to interrogatories propounded to the defendant, Maxime H. Furlaud, the following appears as a list [fol. 157] of the stockholders of the corporation from the 1st day of February, 1930, to the time of its dissolution, October 27th, 1931, with a statement of the number of shares held by each stockholder:

Preferred Stock

Maxime H. Furlaud, from August 1, 1928 to July 29, 1930, 5,000 shares.

Furlaud Holding Corporation, from July 29, 1930, 5,000 shares.

Common Stock

Maxime H. Furlaud, from August 1, 1928 to April 4, 1930, 1,200 shares.

Carlos Reuter, from August 1, 1928, 800 shares.

Otto E. Schuller, from April 4, 1930 to July 29, 1930, 1 share.

Maxime H. Furlaud, from April 4, 1930 to April 15, 1930, 1,199 shares.

Carlos Reuter, from April 15, 1930, 200 shares.

Maxime H. Furlaud, from April 15, 1930 to July 29, 1930, 999 shares.

Furlaud Holding Corporation, from July 29, 1930, 1,000 shares.

The following is a list of each and every director of Furlaud & Company, Inc. (otherwise known as Furlaud, Reuter & Co., Incorporated and Winchelsea Holding Corporation) from the 1st day of February, 1930, to the time of its dissolution:

M. H. Furlaud, from February 1, 1930 to October 27, 1931.

[fol. 158] Carlos Reuter, from February 1, 1930 to October 27, 1931.

F. T. Kelsey, from February 1, 1930 to August 1, 1930.

J. P. Cleaver, from August 1, 1930, to February 21, 1931.

Robert Halporn, from February 21, 1931 to October 27, 1931.

The following is a list of each and every officer of Furlaud & Company, Inc. (otherwise known as Furlaud, Reuter & Co., Incorporated and Winchelsea Holding Corporation) from the 1st day of February, 1930 to the time of its dissolution:

President, M. H. Furlaud, from February 1st, 1930 to October 27, 1931.

1st Vice Pres., Carlos Reuter, from February 1, 1930, to October 27, 1931.

Treasurer, M. H. Furlaud, from February 1, 1930 to August 1, 1930; Robert Halporn, from August 1, 1930 to October 27, 1931.

Secretary, John W. DeWitt, from February 1, 1930 to August 1, 1930; J. P. Cleaver, from August 1, 1930, to February 21, 1931; Robert Halporn, from February 21, 1931 to October 27, 1931.

Asst. Vice-Pres., R. S. Cullen, from January 2, 1931 to June 30, 1931; C. H. Drew, from January 2, 1931 to June 30, 1931; O. E. Schuller, from December 31, 1930 to October 27, 1931.

Cullen and Drew had an entirely independent firm prior to becoming employees of Furlaud & Company. The trans-
[fol. 159] action was finished before they became employees. They did not become officers until January 2, 1931.

W. A. Lee, from January 2, 1931 to August 31, 1931.

Robert Halporn, from December 31, 1930 to October 27, 1931.

Asst. Secretary, Robert Halporn, from August 1, 1930 to February 21, 1931.

Asst. Treasurer, J. P. Cleaver, from August 1, 1930 to February 21, 1931.

J. P. Cleaver never was an employee of Furlaud & Company. He was connected with Furlaud Holding Corporation, the stock of which was owned by Mrs. Furlaud. Mrs. Furlaud owns 10,000 shares of Byron Corporation, and Kipling Corporation owns the other 30,000 shares.

F. T. Kelsey and James P. Cleaver were nominees of Maxime H. Furlaud.

Robert Halporn was the joint nominee of Maxime H. Furlaud and Carlos Reuter.

The situation of Maxime H. Furlaud and Carlos Reuter is self explanatory.

John W. DeWitt and Jas. P. Cleaver were nominees of Maxime H. Furlaud.

R. S. Cullen, C. H. Drew, W. A. Lee, Robert Halporn and Otto E. Schuller were employees of Furlaud & Company, Inc.

Chaucer Corporation has never been dissolved.

The following is a list of every stockholder of the defendant Chaucer Corporation from February 1st, 1930 to date, together with a statement of the number of shares held by each stockholder.

Elsie Reuter, from May 10, 1930, 10,000 shares.
[fol. 160] Virgil Corporation, from May 15, 1930, 30,000 shares.

The following is a list of the directors of the defendant Chaucer Corporation from February 1, 1930 to date:

Carlos Reuter.
Tillie Pollack, up to August 27, 1931.
Paul M. Coonrod.
Elsie Reuter, from August 27, 1931.

The following is a list of the officers of Chaucer Corporation from February 1, 1930, to date:

President, Carlos Reuter.
Treasurer, Paul M. Coonrod, up to August 27, 1931.
Treasurer, Elsie Reuter, from August 27, 1931.
Secretary, Paul M. Coonrod.

Kingston Corporation has never been dissolved.

CHARLES C. NUSS, recalled, testified as follows:

Direct examination.

By Mr. Royall:

The additional properties mentioned by Mr. Duke were all in the nine properties that were referred to by Mr. Duke, as separate properties.

There were, however, three properties that were not covered by escrow purchases; these were the Tucker acreage, the C. P. Levier, and the W. G. Wade. The Stybr-Watson property, consisting of 14,000 acres, was in escrow, but was treated separately in the report. That is the property which [fol. 161] I testified in my direct examination was conveyed gratuitously. The total appraisal of the Nuss escrow, which included the Stybr-Watson and the Wade properties, was $2,637,164. The purchase price of the Nuss properties was $660,000, and of the Wade property $5,135. The Tucker property consisted of leases on approximately 765 acres of unoperated territory for which $12,000 was paid. The Levier consisted of 5,500 acres of unoperated land, and cost approximately $11,800.

The Wade property, consisting of 1,000 acres and costing $5,135, was treated as part of the Nuss appraisal.

Q. I think you have testified that the Nuss property, including this Stybr-Watson acreage you gave, and this Wade acreage, that was additionally acquired; what was that valued at?

Mr. Hirshfield: Again may I renew my objection on all of the grounds previously stated?

The Court: Yes.

Mr. Hirshfield: Exception.

The Court: Yes, you may have an exception to this line of testimony.

Mr. Royall: The witness may answer the question?

The Court: Yes.

A. The valuations of the two properties you mentioned, Stybr-Watson and the W. G. Wade including operated property, approximately $2,000 or $3,000.

The Tucker ad Levier undeveloped acreage were attached to the Behm property. The Behm property, with those

[fol. 162] additions, were appraised at $1,596,550. The purchase price of the Behm property was $200,000. The Tucker property cost $5,000 and the Levier cost $11,800.

Prima Facie Proofs Closed.

Defendants' Proofs

ROBERT HALPORN, called as a witness on behalf of the defendants, testified as follows:

Direct examination.

By Mr. Hirshfield:

I was an officer of the Winchelsea Corporation, formerly Furlaud, Reuter & Company, and formerly Furlaud & Company, Inc. I was formerly an officer of Kingston Corporation; I was present at the closing of the Duquesne Gas Company matter on April 9th, 1930, and I had charge under Mr. Reuter of the financial arrangements at that time.

On April 9th, 1930, Furlaud & Company borrowed from the Chatham & Phenix National Bank & Trust Company $700,000 against the collateral of $1,000,000 par value notes of Duquesne Gas Company, and some stock; I cannot tell you the exact number of shares. This money was put into the account of Furlaud & Company with the Central Hanover Bank & Trust Company, and this $700,000, together with other moneys, were used to pay off the day loan of the Central Hanover Bank & Trust Company. Furlaud & Company, on the same day, borrowed $300,000 from the Hibernia Trust Company against collateral consisting of [fol. 163] Duquesne bonds. This loan was applied similarly. On the same day Furlaud & Company borrowed $500,000 from the Pacific Trust Company, against collateral consisting of Duquesne bonds, which loan was applied similarly.

I believe that the Pacific Trust Company loan and the Hibernia loan were paid off in the course of three months and the Chatham & Phenix loan a little bit later.

I was an officer of the Duquesne Gas Company. I have made an examination of the preliminary original stock certificate book of the Duquesne Gas Corporation; I was one of the signing officers of all the shares of original issue

and can say of my own knowledge that the sole stockholder of Duquesne Gas Corporation on April 9th, 1930 and April 10th, 1930, was F. L. Parisette, who was the nominee of Kingston Corporation and Furlaud & Company, Inc., and an employee of Furlaud & Company, Inc.

I know that he was the nominee inasmuch as I was an officer of Kingston Corporation and Furlaud & Company, Inc. It was the custom to put all stock held by Furlaud & Company in the name of F. L. Parisette, and we used his name as a "Street Name". Stock was put in a "Street Name", namely, of one F. L. Parisette to facilitate the transfer of stock owned by the corporation, which would otherwise have necessitated a corporate resolution for each transfer.

Original stock certificate book of Duquesne Gas Corporation was offered in evidence and marked "Defendants' Exhibit B".

I know of my own knowledge that Furlaud & Company, Inc. was sole stockholders of Kingston Corporation on April 9th, 1930.

[fol. 164] Minute book of Kingston Corporation was offered in evidence and marked Defendants' Exhibit C.

One share of stock of Kingston Corporation was held in Mr. Furlaud's name, and one share of stock was held in my name, as nominee of Furlaud & Company, Inc. When a dividend was declared of $5,500 on each share of stock, and checks of $5,500 a piece were issued to each of us, those checks both went into the account of Furlaud & Company, Inc.

Certified copy of Certificate of Incorporation of Furlaud & Company, Inc. was offered in evidence and marked Defendants' Exhibit D.

I was present at the closing of April 9th, 1930, and had occasion to see the checks that came in from the various members of the "Distributing Group"; all those checks were made payable to the order of Furlaud & Company, Inc., and they were deposited with the Central Hanover Bank & Trust Company in the account of Furlaud & Company, Inc.

Q. Mr. Halporn, I requested you to look at the books of Furlaud & Company recently to make an inspection

thereof, with reference to the number of bonds that were taken up and paid for on April 9th, 1930; can you state from your own knowledge, as refreshed by those books, how many bonds were taken up on that day?

A. Approximately $2,000,000 face value of bonds.

Q. Have you refreshed your recollection as to the amount of the "Commitments" that were made up by various sub-[fol. 165] scriptions to the distributing group on April 9, 1930?

A. Yes.

Q. Will you state what the total amount of the subscriptions, face value of bonds that were made by that time?

A. Approximately $2,350,000 nominal value.

Mr. Hirshfield: I read from the certificate of incorporation of Furlaud & Company, Inc., paragraph 3, relating to the purposes for which it is to be formed, which are as follows:

"To institute, enter into, conduct, assist in promoting, participating in, invest in, carrying on and engage in mining, quarrying, irrigating, stock-raising, real estate, engineering, contracting, manufacturing, industrial, commercial, mercantile, construction and development enterprises, ventures, operation, contracts, works and businesses of every nature, name and description in any part of the world, and so far as permitted by law, within the State of New York.

"To promote and assist financially or otherwise corporations, firms, syndicates, associations, individuals and others and to aid all or any of them by loans, subsidy, guarantee or in any other manner whatsoever."

Cross-examination.

By Mr. Royall:

Mr. Furlaud and Mr. Reuter were present at the closing on April 9th, 1930. Mr. Furlaud was president of the corporation; I felt that both Mr. Reuter and Mr. Furlaud were [fol. 166] my bosses, I would not say who was the big boss. I am an employee of Furlaud & Company, Inc., and received a salary of $400.00 a month.

I received in addition a bonus of $7,500. I did not get any special bonuses in respect to special transactions, and I did not receive any other money. I was Mr. Furlaud's

and Mr. Reuter's chief assistant in financial details. No one in the organization knew more about and had closer contact with the financial arrangements respecting this issue than I had.

Q. You have testified that the proceeds of the $700,000 Chatham & Phenix Loan, of the $300,000 Hibernia Loan and the $500,000 Pacific Trust loan, all negotiated by Furlaud & Company, Inc. on April 9th, were deposited on that day to the credit of Furlaud & Company, Inc. with the Central Hanover Bank & Trust Company, is that right?

A. Yes.

Q. And thus applied to the liquidation of the $3,379,500 loan, that one-day loan, that Mr. Furlaud had negotiated at the Central Hanover Bank & Trust Company?

A. Furlaud & Company.

Mr. Furlaud negotiated the making of that loan.

Q. What became of the checks that were delivered at the closing on April 9th, 1930, at the Central Hanover Bank & Trust Company by the subscribers against the delivery of the bonds which they had subscribed for; what disposition was made of those checks?

A. They were endorsed by Furlaud & Company, Inc. and deposited with the Central Hanover Bank & Trust Company.

Q. Now, as a result of those various deposits—one other question first—is it not a fact that two checks were also passed on April 9th against the account of the Kingston [fol. 167] Corporation at the Central Hanover Bank & Trust Company to the order of Furlaud & Company, Inc., aggregating the sum of $565,100?

A. That is right.

Q. So that there was passed a credit of Furlaud & Company on that date of $565,100, which came back to the Kingston Corporation, the proceeds of the loans from the Chatham, Hibernia and Pacific and the checks that the subscribers to the bonds turned over there; how much was left in the account after crediting those things and charging the loan against it?

A. In whose account?

Q. Furlaud & Company's account.

A. Well, I had occasion since this to look up the account——

Q. How much was that account?

A. Approximately $500,000.

Q. So after those credits were completed, there were approximately—I presume you are here prepared to testify what you got in exact figures, are you not?

A. Will you permit me to get my books?

The Court: Yes.

Mr. Royall: Certainly, we want exact figures.

The Witness: The statement of account shows on April 9, 1930, a balance of $482,782.02 to the credit of Furlaud & Company, Inc.

Q. What did the balance on the next day show?

A. The balance on April 10th shows $286,782.02.

Q. What was withdrawn during the interval?

A. I beg pardon.

Q. What withdrawal was made during the interval?

Mr. Hirshfield: I object to that as improper cross-exam-
[fol. 168] ination, unless Mr. Halporn is made his own witness.

The Court: I will allow it.

Mr. Hirshfield: Exception.

By the Court:

Q. What happened to this sum of approximately $200,000?

A. One check was drawn for $70,000, one for $125,000 and one for $1,000.

Q. Do you know to whom these checks went?

A. There was one check to the order of the Pacific Trust Company for $1,000.

By Mr. Royall:

Q. Yes, how about the rest of them?

A. There was one check for $70,000 to the Hibernia Trust Company.

Q. Yes?

A. And one check for $125,000 to the Chatham & Phenix National Bank & Trust Company.

Q. So that at that very moment their loans had been liquidated to the extent of the credit of those checks, hadn't they?

A. I beg your pardon. These checks $70,000 and $125,000 were not used to pay off loans to the Hibernia Trust Company.

By the Court:

Q. What were they used for?

A. They were credited to our regular account with the Chatham & Phenix National Bank & Trust Company and Hibernia Trust Company.

Q. That is, the regular account of Furlaud, Reuter & Company to the deposit account?

A. Of the deposit account, that is correct.

[fol. 169] By Mr. Royall:

Q. You had to do with the organization of the distributing group; you were in close touch, weren't you, with the operation of the marketing of these bonds?

A. I was no salesman.

Q. I didn't ask you if you were a salesman or not, I asked you if you were in close touch with the progress of that work and kept advised of it?

A. Yes, I was.

Q. Isn't it a fact that the subscribers to the bonds were required under the syndicate arrangement to take the bonds up on the delivery date by an initial payment of 96½% of the face value of the bonds, subject to future adjustment, is that a fact or not?

A. Yes.

Q. Now, I don't want approximations, I want details. To what extent was the bond subscription subscribed for at the time of the closing?

A. It is impossible for me at this time to give an exact amount, because no records are available to ascertain this amount, but so far as I can recollect, and that is the only thing I can do, it was approximately $2,350,000.

Q. Who were Bioren & Company?

A. A banking firm in Philadelphia.

Q. What did they have to do with the issue of these bonds?

A. They were members of the banking group.

Q. Who were Bradford, Kimball & Company?

A. They were a banking house in San Francisco and Los Angeles.

Q. What did they have to do with the issuance of these bonds?

A. They were also in the banking group.

Q. Who were Hinks Bros. & Company?

[fol. 170] A. They were a banking house in Bridgeport, Connecticut.

Q. What did they have to do with this?

A. They were also members of the banking group.

Q. Who were G. H. Huston & Company, Inc.?

A. They were bankers in New York.

Q. What did they have to do with it?

A. They too were members of the banking group.

Q. You say all these five houses were members of the banking group. Do you make any distinction between them as a banking group and the subscribers and the distributing group, do you make any distinction between subscribers and distributing group?

A. There is a distinction.

Q. Is there a distinction?

A. There is a certain distinction.

Q. All right, tell the Court what the distinction is.

A. The members of the banking group are really each of them in control of certain territory in which bonds are being sold. For example, Bioren & Company had reserved for themselves the district of Philadelphia.

Q. How many of the bonds were allotted to Bioren & Company as a member of the banking group?

A. I can not tell you that; I don't remember.

Q. Give us your best recollection. Have you anything that you can refresh your recollection by?

A. I would have to look through the books of Furland & Company, Inc. to see how many bonds they paid for.

Q. Give us your best recollection.

A. I would say a million dollars.

Q. All right, as to Bradford, Kimball & Company, how much of the issue was allotted to them?

A. I don't remember that.

[fol. 171] Q. Give us your best recollection on that?

A. I would say about $250,000.

Q. Hinks Bros. & Company, how many were allotted to them?

A. About $300,000.

Q. Huston?

A. About $150,000.

Q. Now, as a matter of fact, Mr. Halporn, didn't this banking group commit themselves to take the whole $4,000,000, as a banking group? Please answer the question, Mr. Halporn.

A. No.

Q. What was the function of the banking group?

A. Well, in this case, the banking group was just the wholesale distributing group.

Q. Have you ever had any experience with public issues before, or is this the only one you know about?

A. I have had experience before.

Q. Have you had enough experience in this matter to know what the ordinary function of a banking group is in a public issue?

A. The ordinary function of a banking group was to underwrite the entire issue.

Q. Quite so. And that is what happened here, isn't it?

Mr. Hirshfield: Just a minute, I object to that.

The Court: He may answer whether there was any underwriting agreement, or whether it was one of these fly-by-night transactions that took place in the heyday of prosperity.

By the Court:

Q. What was it, did the banking group undertake to float the whole issue?

A. No.

Q. What was it? Did they say they would take so many bonds, and if they did not take it, what happened?

[fol. 172] A. They agreed to take a certain number of bonds, but they did not guarantee the complete issue.

Q. Did they all make good on their agreements to take a certain number of the bonds and dispose of them, each of them?

A. They did.

Q. What was the aggregate of the amount that they took and disposed of?

A. Just as I told you before, I can not exactly remember.

Q. Where are the papers which show that?

A. The way to show it is through the books of Furlaud & Company.

Q. Are they here?

A. They are here.

Q. Can you find out and tell us from that what it is?

Mr. Hirshfield: We tried to get that information and Mr. Halporn spent quite a few hours trying to get that.

The Court: Can you check that up and get that information if I adjourned until two o'clock? Is there any other point you want?

Mr. Royall: Yes, your Honor, and I think it will throw a great deal of light on this subject of the bankers' group letter——

The Court: Have you got that?

The Witness: There was no banking group letter.

Mr. Hirshfield: Furlaud & Company organized the syndicate and they wrote a letter—I have been through all of this procedure, your Honor—it is a kind of copy-cat method that all of these bankers use. These bankers did not allow their names to be signed.

Mr. Royall: I would like to see those letters.

[fol. 173] Mr. Hirshfield: We simply haven't got them.

The Court: Are any of these bankers still in business?

Mr. Hirshfield: Yes, but they are in San Francisco, Los Angeles, Philadelphia and so on.

Recess.

Mr. Hirshfield: I think he has acquired the information about which I asked and about which Mr. Royall was asking him as to amount of bonds that Bioren & Company and the other people took. Have you got that?

The Witness: Yes.

Mr. Hirshfield: All right, give it to us.

The Witness: Bioren & Company took up $442,000 and paid for it; Hinks Bros. for $315,000; C. H. Huston & Company $275,000 and Bradford, Kimball & Company for $175,000.

Cross-examination.

By Mr. Royall (continued):

Q. That represented the balances of their undistributed commitments, did it not?

A. This represents the amount of bonds that were delivered to them and paid for by them.

Q. Yes, but the amount was arrived at as an undistributed balance of their commitments, wasn't it?

A. Well, as I told you before, the records available here only show how many bonds were paid for by each of these houses.

By the Court:

Q. Did they take a commitment for a certain number of bonds that they did not handle?

[fol. 174] A. Bioren had a territory in Philadelphia and there were bonds delivered in Philadelphia for which Bioren was to receive the credit.

Q. And are those bonds included in this?

A. No, they are not included here. As I told you, I can not, by this record state on whose order these bonds were delivered.

By Mr. Royall:

Q. Now, kindly answer my question.

A. What is your question?

Q. Is it a fact that these amounts that you read just now represented the balances in the case of each banker, of their undistributed commitments. Do you understand that phrase as I use it?

A. No, I don't understand it.

Q. All right, I will explain it in another way. There were numerous members of the distributing group, were there not?

A. There were.

Q. Perhaps 30 or 40 different houses?

A. There were.

Q. And the distributing groups revolved around members of the banking group, that is the distributing group, what you speak of as the Philadelphia or Pennsylvania area and they were revolving around Bioren & Company, am I right?

A. Yes.

Q. And the distributing houses located on the Coast, California and the western coast of these United States, were revolving around San Francisco, the house—what was their name, the Kimball firm, isn't it?

A. Yes, sir.

Q. They revolved around Bradford, Kimball & Company?

A. That is correct.

Q. And Hinks Bros. & Company was another circle of distributors?

A. As far as I remember, in the case of Hinks Bros. all [fol. 175] the bonds that were delivered to Hinks were bonds that they subscribed for, that they were committed for.

Q. Let me see if I can get this: There were received numerous checks at the closing on the 9th from numerous houses in and about Pennsylvania——

A. Yes.

Q. Which paid for bonds, when delivered, to the credit and the commitment of Bioren & Company, isn't that right?

A. Yes.

Q. So that this Bioren & Company payment represented the balance of Bioren & Company's undistributed commitment; now do you understand my phrase?

A. Yes.

Q. That is the fact, isn't it?

A. That is the fact, but may I add something?

The Court: Yes.

The Witness: There were undoubtedly bonds sold to houses in Philadelphia beyond the commitment of Bioren & Company.

By the Court:

Q. But you gave them the credit?

A. Right.

By Mr. Royall:

Q. That generally describes the method that was employed in this case?

A. Yes.

Q. And it is fair to say then that these figures that you have written out represent what they took, to take up the balance of their commitments?

A. As I stated, that is not quite correct.

Q. Isn't it correct?

A. It is not correct, because more bonds were taken up than were committed by Bioren.

By the Court:

Q. That is, they agreed to underwrite, as it were, a certain number of bonds?

A. Yes.

[fol. 176] Q. They had other houses in the Philadelphia area which handled some of the bonds and Bioren's commitment was reduced to the extent that those other houses took them up?

A. Yes, and in addition to that——

Q. And in addition to that you sold some bonds in the Philadelphia area?

A. Yes.

Q. For which you gave Bioren credit?

A. Yes.

Q. When, after all is said and done, they paid for the amount of bonds that you committed to them?

A. Yes.

By Mr. Royall:

Q. So their commitment was fully discharged, if it was a million dollars?

A. Yes.

Q. And you don't know whether it was a million, a million and a half or two million dollars, and you would not say that?

A. No, I cannot say.

Q. You don't know that?

A. No, but all the commitments were discharged.

Kingston Corporation opened an account with the Central Hanover Bank & Trust Company by a deposit of $27,000 which was furnished by Furlaud & Company, Inc. The purpose of that transaction was probably to pay out certain amounts by Kingston Corporation; then $3,015,000 was credited to that account on April 9th, and then, at a later time, there was paid out $2,449,000 to take up the escrow deposits. Out of this account on April 9th, there was paid to Furlaud & Company, Inc., $565,100, and some two or three months later there came into the treasury of Kingston some payments made by the Byron Corporation and Chaucer Corporation amounting to $260,000 or $265,000 which was in payment for stock. The money that was in the treasury of Kingston Corporation, after these trans-[fol. 177] actions were completed, but not all of it, was paid over to Furlaud & Company, Inc., by way of a dividend. I have not the books of Kingston here, but the statement of the Central Hanover Bank & Trust Company shows a balance to the credit of Kingston Corporation of $6,400.07,

after paying $275,000 in dividends in December. All of the $275,000 was ultimately paid over to Furlaud & Company.

A secondary distributing group was organized and approximately 200 or 300 bonds were the subject matter of that secondary distributing group.

All of the $4,000,000 bonds got sold. Furlaud & Company, Inc. bought $1,194,000 bonds by miscellaneous purchases.

These miscellaneous purchases were made up to July 23rd, 1931.

There was trading in these bonds before August, 1930, by Furlaud & Company, Inc. under the first syndicate agreement. We were permitted to re-deliver bonds at repurchase cost. Some of our distributors failed to take up these bonds, and then we were left with a certain number of bonds which became the subject of the secondary distributing group. I believe that the bonds were all marketed as a result of the operation of the secondary distributing group. All the $4,000,000 bonds and the $1,194,000 bonds acquired by miscellaneous purchases were marketed.

At the time of the closing, we did not have sufficient amount of commitments on hand, and we had to borrow money in order to close.

The subscriptions that had come in before we had our closing, indicated that the issue would go over satisfactorily.

Of the $565,000 paid by Kingston Corporation to Furlaud & Company, Inc. $300,000 were paid over to Furlaud & Com- [fol. 178] pany, Inc. for expenses, under a written agreement between Furlaud & Company, Inc. and Kingston Corporation. The agreement provided that Kingston Corporation should reimburse Furlaud & Company, Inc. for all expenses, I have not the agreement and I don't know whether it says $300,000 and no more, or up to $300,000. The $300,000 was deposited with the Central Hanover Bank & Trust Company by Furlaud & Company, Inc. to the account of Furlaud & Company, Inc.

By Mr. Royall:

Q. Do you know what the actual expenses of Furlaud & Company were in connection with this?

A. I don't know.

Q. You don't know whether they were more or less than $300,000?

A. I think they were somewhat less than that.

Mr. Hirshfield: May I state, your Honor, not knowing the two issues were coming up, we were unprepared first, on the question of appraisal, and second, on the question of expenses and losses and profits. There was nothing in the bill that gave us any notice of that.

Mr. Royall: We ask for an accounting.

Mr. Hirshfield: Yes, you ask for an accounting, but——

Mr. Royall: What I am trying to do is cross examine the witness. May I continue my cross-examination, your Honor?

The Court: Go ahead.

Q. Have you anything here by which you can enable yourself to testify with any degree of accuracy as to this?

[fol. 179] A. I believe the books of Furlaud & Company would show.

Q. Are you able, without any delay, to get that information?

A. I would have to look at the expenses.

Mr. Royall: What does your Honor wish to be done?

The Court: He was paid this much money. If you get an accounting, that will be ascertained in the accounting.

Mr. Royall: What we would like to accomplish is to make up our decree here, rather than go to a Master.

The Court: If you got to a Master, you would be allowed such sum of money as would represent the reasonable cost of handling the situation.

Mr. Royall: The Court could do that better than a Master.

The Court: Well, I am not going to do it now.

$300,000 was the estimated amount that would include the attorneys' fees, commissions to agents who had brought these properties to the attention of Kingston, printing fees and preparations of stocks, bonds and notes, engineers' fees, auditors' fees and recording fees. Out of this money approximately $17,000 or $18,000 was paid to both engineers. The attorneys' fees were not known at this time, but they were fixed at $30,000.

Of the $565,000 paid to Furlaud & Company, Inc. by Kingston on April 9th, Kingston loaned $265,100 to Fur-

laud & Company, Inc., and the check was deposited for the [fol. 180] account of Furlaud & Company, Inc. by the Central Hanover Bank & Trust Company. I don't think the loan was ever repaid.

Redirect examination.

By Mr. Hirshfield:

Furlaud & Company, Inc. was dissolved on October 27, 1931 prior to the commencement of this suit. The loans which were made at the three banks were arranged prior to the closing and were made after the closing.

By Mr. Hirshfield:

Q. Mr. Halporn, you made some calculations at the court's suggestion during the recess. Will you be good enough to tell the court how much actual money was received on April 9, 1930, by Furlaud & Company?

A. Furlaud & Company received $1,500,000 from the three loans, as stated before, $300,000 plus $265,100 from Kingston Corporation and $1,866,330 from the taking up of $2,500,000 of bonds, being a total of $3,931,430.

Mr. Hirshfield: That is all.

Recross-examination.

By Mr. Royall:

Q. Let us see if those figures check out. You say at the end of that day they had $484,000?

A. $482,000.

Q. They had $482,000 left in the bank?

A. Yes.

Q. Now, they had given a check on that day of $3,379,500 to Duquesne Gas Corporation, had they not?

A. Correct.

Q. And through the route of Kingston Corporation on [fol. 181] that day, they had gotten back $565,100 of that money?

A. They received from Kingston $565,100.

Q. They received back $565,100 of that money that they had——

Mr. Hirshfield: I object to the word "back."

The Court: That amount was paid by Kingston.

Q. $3,379,500 they paid out on that day?
A. Yes.
Q. And then they had left how much?
A. $482,000.
Q. There is $3,861,000. You say they received $1,500,000 from the three banks?
A. Yes.
Q. And that they got $565,100 from Kingston?
A. Which makes $2,065,100.
Q. According to that, they got $1,795,900 from other sources; did that check with your figures?
A. $1,866,330.
Q. Your records show they got $1,866,330 on that day?
A. Yes.
Q. From the take-up by miscellaneous distributing houses of bonds on that day?
A. Yes.
Q. Now then, let me ask you this further question: Day by day, after that, immediately following that, distributing houses were taking up bonds, were they not?
A. Yes.
Q. Actively?
A. Yes, sir.

Defendants' Exhibit E was offered in evidence, consisting of minutes of organization meeting of Duquesne Gas Corporation, attached to the answers of complainant to the interrogatories propounded by defendants.

[fol. 182] Defendants' Exhibit F was offered in evidence, consisting of minutes of meetings of directors of Duquesne Gas Corporation attached to the interrogatories answered by complainant.

Defendants' Exhibit G was offered in evidence, consisting of minutes of stockholders' meeting of Duquesne Gas Corporation.

Defendants' Exhibit H was offered in evidence, consisting of the offer of Furland & Company, Inc. to Duquesne Gas Corporation.

Motion by the defendants to dismiss on behalf of each and every of these defendants. Motion taken under advisement by the Court.

[fol. 183] PLAINTIFF'S EXHIBIT 1

UNITED STATES DISTRICT COURT, FOR THE SOUTHERN DISTRICT OF NEW YORK

FRANK T. HARRINGTON, Complainant,

against

DUQUESNE GAS CORPORATION, Defendant

PETITION OF GEORGE W. MCCANDLESS

To the Honorable Judge of the United States District Court for the Southern District of New York:

The petition of George W. McCandless, Receiver, shows to this Honorable Court:

First: That on the 19th day of January, 1932, your petitioner by a per curiam decree duly made by the United States District Court for the Western District of Pennsylvania, was duly appointed receiver of the assets, lands, tenements and hereditaments of the defendant, the Duquesne Gas Corporation, and all of its property, real and personal, including choses in action, and was required to file a bond in the penal sum of Fifty thousand dollars ($50,000).

Second: That your petitioner has duly accepted the trust in him reposed and has duly filed a bond as directed by said decree.

Third: That defendant is a corporation organized under and existing by virtue of the laws of the State of Pennsyl- [fol. 184] vania, with its principal office in the City of Washington, Washington County, Pennsylvania, and that its principal business is the business of producing and selling natural gas.

Fourth: That the aforesaid decree appointing your petitioner as receiver, was granted upon the amended bill of complaint in the above-entitled action, duly filed in the United States District Court for the Western District of Pennsylvania, upon the answer of the defendant Duquesne Gas Corporation to said amended bill of complaint. Attached hereto and made a part hereof are exemplified copies of said amended bill of complaint, said answer and the decree appointing your petitioner receiver in said suit in the United States District Court for the Western District of Pennsylvania.

Fifth: That by the aforesaid decree the above entitled action was consolidated with an action brought in the District Court of the United States for the Western District of Pennsylvania by the Central Hanover Bank and Trust Company, as trustee under the first mortgage of the Duquesne Gas Corporation against said Duquesne Gas Corporation, and said decree appointed your petitioner as receiver in the consolidated action and that at all times subsequent to his qualification your petitioner has acted as receiver in the consolidated action.

Sixth: That the solicitors for said Frank T. Harrington, said Duquesne Gas Corporation and said Central Hanover Bank and Trust Company, as trustee, consented to the entry of said decree.

[fol. 185] Seventh: That on the basis of investigations conducted by your petitioner, your petitioner believes that the Duquesne Gas Corporation has a good cause of action against the promoters of defendant Duquesne Gas Corporation including Maxime H. Furlaud and Carlos Reuter for an accounting and for the restitution of funds fraudulently diverted and misappropriated and of secret and excessive profits. Your petitioner as such receiver has retained the firm of Ehrich, Royall, Wheeler & Walter of the City of New York to take such proceedings as are necessary and proper for the purposes of bringing such suit in this district.

Eighth: That your petitioner is informed that said Maxime H. Furlaud and Carlos Reuter are residents of the County of New York which lies within the territorial limits of the District Court of the United States for the Southern District of New York.

Ninth: That your petitioner verily believes that it is necessary for the protection of the interests of the creditors and stockholders of said Duquesne Gas Corporation and for the interest of the corporation itself, that an ancillary receiver be appointed by this court for the purpose of instituting such action in this district.

Tenth: That no previous application for the relief herein sought has been made.

Wherefore, your petitioner prays for a decree of this court appointing an ancillary receiver of Duquesne Gas Corporation in and for the Southern District of New York

[fol. 186] with all rights and powers to carry into force and and effect the decree of the court of original jurisdiction, and to bring an action against said promoters for an accounting and for the restitution of funds fraudulently diverted and misappropriated and of secret and excessive profits, and to petition for an order to retain solicitors for that purpose; and to do any and all things necessary in connection therewith for the protection of the interests of the estate; and restraining the defendant, its agents, servants, attorneys, creditors and stockholders, and all persons from interfering in any manner with said ancillary receiver in effecting such purposes.

Dated, New York, March 23, 1932.

George W. McCandless, Petitioner.

(Verified by George W. McCandless on March 23, 1932.)

[fol. 187] UNITED STATES DISTRICT COURT, FOR THE SOUTHERN DISTRICT OF NEW YORK

FRANK T. HARRINGTON, Complainant,

against

DUQUESNE GAS CORPORATION, Defendant

AFFIDAVIT OF GEORGE W. McCANDLESS

STATE OF NEW YORK,
County of New York, ss:

George W. McCandless, being duly sworn, deposes and says: I am the petitioner in the annexed petition; to the best of my knowledge there are no suits now pending against the defendant corporation for the appointment of a receiver save as set forth in said petition and save that an application has been made for the appointment of an ancillary receiver in the United States District Court for the District of West Virginia but that said application has not been prosecuted as it was discovered that your deponent's supposition that the defendant corporation owned property in West Virginia was erroneous.

George W. McCandless.

Sworn to before me this 23rd day of March, 1932.

Hazel E. Applegate, Notary Public.

[fol. 188] IN THE DISTRICT COURT OF THE UNITED STATES, FOR THE WESTERN DISTRICT OF PENNSYLVANIA

No. 2554 in Equity

FRANK T. HARRINGTON, Complainant,

against

DUQUESNE GAS CORPORATION, Defendant

AMENDED BILL OF COMPLAINT, ANNEXED TO PETITION OF GEORGE W. McCANDLESS

To the Honorable the Judges of the District Court of the United States for the Western District of Pennsylvania:

The complainant for himself and all other stockholders, bondholders, noteholders and creditors of the defendant corporation, who, being interested in the subject matter of this suit should become parties complainant hereto and contribute to the expenses hereof, brings this, his amended bill of complaint:

1. The complainant re-affirms the allegations contained in the first paragraph of his bill of complaint as filed to the effect that this is a suit of a civil nature in equity wherein there is involved a controversy wholly between citizens of various states and wherein the matter and amount in controversy, exclusive of interest and costs, exceeds the sum or value of $3,000.00.

[fol. 189] 2. The complainant re-affirms the allegations contained in the second paragraph of his bill of complaint to the effect that he is a resident and citizen of the City of New York, in the State of New York, and is the owner of 100 shares of non-assessable common stock without nominal or par value, of the defendant corporation. He further avers that although the stock has been but recently transferred into his name, he has been the actual owner of the same in the name of Henry B. H. Ripley since September 5, 1930.

3. The complainant further avers that the defendant is a public utility corporation organized under the laws of the State of Pennsylvania in the year 1930 and at the present time has its principal office in the City of Washington, Washington County, Pennsylvania.

4. The complainant avers upon information and belief that the stockholders, bondholders and noteholders of the defendant are very many in number and are citizens and residents of many states in the United States and for that reason it is impossible for the complainant to join them in this action and the complainant brings this action not only for his own benefit, but also for and on behalf of all other stockholders, bondholders and noteholders of the defendant and in order that their respective rights and equities may be preserved and protected.

5. That the said defendant corporation has an authorized capital stock of Five million (5,000,000) shares without nominal or par value and that it has issued up to the present time six hundred and ninety thousand (690,000) of [fol. 190] said shares. It further avers that the said defendant corporation owns or operates, either directly or through its subsidiaries, natural gas properties in Pennsylvania and West Virginia.

6. The complainant is informed, believes and therefore avers that practically all of the defendant corporation's gross income since its incorporation has been derived from the transportation, distribution and sale of natural gas to public utility corporations and industrial enterprises, and through a subsidiary to domestic consumers, all in the vicinity of the City of Pittsburgh.

7. The complainant is informed, believes and therefore avers that the principal assets of the defendant corporation are the property owned or leased, managed and operated through it and its subsidiaries consisting of over one hundred and twenty-five (125) gas wells in approximately fourteen thousand (14,000) acres of gas properties within a radius of from seven (7) to forty-five (45) miles of the City of Pittsburgh, and that it further owns pipe, equipment, machinery, etc.

8. The liabilities of the said defendant corporation are as follows:

(a) Four million ($4,000,000) Dollars First (closed) Mortgage 6% Convertible Gold Bonds, dated March 15, 1930, and which bear interest at the rate of 6% per annum, payable March 15th and September 15th in every year,

aggregating at the present time $3,965,000. and will mature March 15, 1945, for the payment of which the defendant [fol. 191] corporation is distinctly liable. That interest on the said bonds due September 15, 1931, is in default and has continued in default for a period of more than thirty days.

(b) One million ($1,000,000) Dollars Convertible 6½% Secured Gold Notes, dated March 15, 1930, maturing March 15, 1935, aggregating at the present time $949,000, for the payment of which the defendant corporation is directly liable. That interest on the said notes due September 15, 1931, is in default and has continued in default for a period of more than thirty days thereafter.

9. That in addition to its inability to provide sufficient reserve with which to meet the above mentioned interest on the first mortgage bonds, the corporation has carried on its business at a loss throughout the year 1930 and 1931.

10. The complainant is informed, believes and therefore avers that the company will continue to operate at a loss even without meeting its interest payments on account of bonds and notes, unless a complete reorganization of its business and affairs is accomplished.

11. The complainant is informed, believes and therefore avers that the defendant will not have sufficient funds to enable its business to be properly continued unless a receiver or receivers be appointed who can borrow the necessary funds subject to the approval of this Court, or in some other manner reorganize the said corporation. That such action is especially necessary in view of the fact that certain contracts which the defendant has entered into can [fol. 192] be realized upon at a profit only if the business, as a whole, can be carried on without interruption; and that unless this Honorable Court in view of the present inability of the defendant to meet its due and maturing obligations, will deal with the properties of the defendant as a whole as a trust fund for the payment of its creditors and stockholders and bondholders as their several interests therein shall appear, such properties will be dissipated, wasted and sacrificed, and interminable litigation will ensue to the great irreparable damage and injury of the complainant

and the creditors and other stockholders, bondholders and noteholders of the defendant.

12. The complainant is informed, believes and therefore avers as follows:

Furlaud Reuter & Company, investment bankers of New York City, arranged the acquisition of the properties now owned or leased by defendant, Duquesne Gas Corporation and did acquire the same at a total cost of $2,527,250. Other expenses were incurred such as engineering, auditing, attorney fees, commissions, etc., amounting to $487,750. and working capital of $365,000. was provided, making total actual costs in connection with the acquisition of the properties of approximately $3,380,000. Title to the properties was taken in Kingston Corporation, a corporation organized by and under the laws of the Commonwealth of Pennsylvania on May 28, 1930 with a directorate identical in personnel to that of defendant upon its organization, both of which corporations were owned and controlled at that [fol. 193] time by said Furlaud, Reuter & Company. The properties were at once transferred to Duquesne Gas Corporation, defendant, at a profit to said Kingston Corporation of approximately $1,500,000.

13. The complainant is informed, believes and therefore avers as follows:

That said Furlaud, Reuter & Company originally employed one Ralph E. Davis, a well known civil engineer, to appraise the various properties to be acquired for the defendant. Pursuant to said employment the said Davis appraised a portion thereof at $1,743,520. and upon his indication that his appraisal of the balance of the properties would be less than $1,000,000, a representative of said Furlaud, Reuter & Company took the data upon which he was working to their offices in New York. Thereupon, and without notice to said Davis, the said Furlaud, Reuter & Company employed the firm of Mattison, Davey & Winters to complete the appraisements, and that firm fixed the figure of $4,929,787. as the appraised value of the said balance of said properties. The complainant is informed, believes and therefore avers that at the present time, with gas reserves, the properties are worth in the aggregate approximately $3,200,000.

14. The complainant is informed, believes and therefore avers as follows:

The said 6% Convertible Gold Bonds in the amount of $4,000,000 at par was sold by the said Furlaud Reuter & Company, and/or their nominees, to the public at $975. each or $3,900,000. and of said sum the defendant corpora-
[fol. 194] tion received the benefit of but $900. each or $3,600,000., the balance being retained by said Furlaud, Reuter & Company and/or their nominees.

15. The complainant is informed, believes and therefore avers as follows:

That the said 6½% Gold Notes in amount $1,000,000. at par, were sold by the said Furlaud, Reuter & Company and/or their nominees to the public at $980. each or $980,-000. and of said sum the defendant corporation received the benefit of but $880. each or $880,000., the balance being retained by said Furlaud, Reuter & Company and/or their nominees.

16. The complainant is informed, believes and therefore avers as follows:

That in the capitalization of the defendant, Duquesne Gas Corporation, the said Furlaud, Reuter & Company caused the total amount of stock, actually issued at that time, to-wit 675,000 shares to be issued to them or their nominees at the stated price in the capital structure of the said defendant of 50¢ per share, or a total of $387,500., some of which said stock was sold by them or their said nominees at various prices up to $9.00 per share, as a result of which said Furlaud, Reuter & Company and/or their nominees acquired a net profit in excess of $800,000., none of which said profit was accounted for or was of benefit to the said defendant, Duquesne Gas Corporation.

17. The complainant is informed, believes and therefore avers that aside from the Bondholders' Protective Commit-
[fol. 195] tee, of which he is a member, and which has filed a petition to intervene in these proceedings, another so-called Bondholders' Protective Committee under the influence of the said Furlaud, Reuter & Company and/or their nominees and associates has attempted to suppress the facts surrounding the fraudulent incorporation and capitalization of the defendant by compelling the trustee

of the said First Mortgage Bonds to bring foreclosure proceedings against the defendant corporation without allowing any opportunity whatsoever for a possible reorganization of the business and affairs of the defendant, and your complainant is informed, believes and therefore avers that in the proceeding to foreclose, petitions to intervene have been or will be filed by the Bondholders' Protective Committee of which he is a member, and which has revoked the authority given to the trustee in the said mortgage indenture, and likewise by certain other noteholders and stockholders of the defendant.

18. The complainant is informed, believes and therefore avers that proceedings have been instituted in a State Court of the State of New York in the City of New York, in which alone can jurisdiction be obtained, against the said Furlaud Reuter & Company, its officers, directors, associates and counsel for restitution of all monies and property improperly converted by them from the credit of said Duquesne Gas Corporation, in which said suit for restitution all stockholders, bondholders, noteholders and creditors of said Duquesne Gas Corporation are or should be interested.

[fol. 196] 19. The complainant further avers that the Bondholders' Protective Committee of which he is a member was on November 24, 1931 permitted by the Public Service Commission of the Commonwealth of Pennsylvania to intervene in proceedings instituted by said Commission against the defendant, Duquesne Gas Corporation, to determine its status as a public utility and to determine whether it has been properly organized, incorporated and financed, and that the said Bondholders' Protective Committee is cooperating with the said Public Service Commission of Pennsylvania in its effort to work out a solution of the affairs of the defendant corporation or to reorganize its business and enable it to continue.

20. The complainant has no adequate remedy at law and only through the intervention of this Honorable Court through the appointment of a receiver or receivers for the defendant corporation can full relief be granted, or the rights of your complainant and other stockholders, bondholders, noteholders and creditors be protected.

Wherefore, the complainant being without adequate remedy at law, and in need of the protection of a Court of Equity in securing his rights respectfully prays as follows:

1. That this Honorable Court appoint forthwith a receiver or receivers of all and singular the property of the defendant corporation, of whatsoever nature, with full power to take into his or their possession, hold and manage the same under the direction of this Court, with such [fol. 197] powers as this Court may from time to time grant in its discretion, to bring suit for, collect, receive and take into his or their possession all the property and assets of the defendant corporation, including its books, records, vouchers, checks, moneys, real estate and all other property, real, personal and mixed; to institute, prosecute, become parties to, intervene, compromise or defend any actions at law, or in equity or in any statute for the recovery, protection and maintenance of any of the assets or properties of the defendant corporation, as he or they may deem proper or necessary, including the institution and prosecution of any such ancillary proceedings as he or they may deem advisable; to settle, collect, compound, adjust or to make allowances upon any debts that may be due or owing to the defendant corporation as he or they may deem proper; to pay any such claims or wages as may have priority, and in general, with all the usual powers of receivers in such cases.

2. That the officers, managers, employees, creditors, stockholders, bondholders and noteholders of the defendant corporation and all other persons, firms and corporations be forthwith required to transfer, convey and deliver up to such receiver or receivers possession of all property of the defendant corporation wheresoever situated.

3. That all persons, firms and corporations be enjoined forthwith from instituting, commencing, prosecuting or continuing the prosecution of any actions, suits, or proceedings at law or in equity or under any statute against defendant corporation, from levying or serving any attach- [fol. 198] ments or executions or other processes upon the defendant corporation save and except the filing of mechanics' or other statutory liens and generally that all persons, firms and corporations be enjoined from doing any

act to interfere with said receivers in their possession of the property of the defendant corporation.

4. That your complainant may have such other and further relief as may be just or proper.

Patterson, Sherrard & Miller, Solicitors for Complainant.

(Verified by Frank T. Harrington, December 31, 1931.)

IN THE DISTRICT COURT OF THE UNITED STATES, FOR THE WESTERN DISTRICT OF PENNSYLVANIA

No. 2554—In Equity

FRANK T. HARRINGTON, Complainant,

vs.

DUQUESNE GAS CORPORATION, Defendant

AMENDMENT TO PRAYER, ANNEXED TO PETITION OF GEORGE W. MCCANDLESS

The complainant for himself and all other stockholders, bondholders, noteholders and creditors of the defendant corporation hereby amends the prayer of his amended bill of complaint so that it shall read as follows:

[fol. 199] 1. That the rights of the complainant and all other stockholders, bondholders, noteholders and creditors of the defendant corporation may be ascertained, decreed and determined; that this Honorable Court will fully administer the fund in which the complainant and all other stockholders, bondholders, noteholders and creditors are interested constituting all the property and assets of the defendant in accordance with the rights, equities, liens and priorities, if any, existing thereon and will enforce and decree the rights, equities, liens and priorities of the creditors, bondholders, noteholders and stockholders of the defendant as the same may finally be ascertained and decreed by this Court.

2. That this Honorable Court appoint forthwith a receiver or receivers of all and singular the property of the defendant corporation, of whatsoever nature, with full

power to take into his or their possession, hold and manage the same under the direction of this Court, with such powers as this Court may from time to time grant in its discretion, to bring suit for, collect, receive and take into his or their possession all the property and assets of defendant corporation, including its books, records, vouchers, checks, moneys, real estate and all other property, real, personal and mixed; to institute, prosecute, become parties to, intervene in, compromise or defend any actions at law or in equity, or under any statute for the recovery, protection and maintenance of any of the assets or properties of defendant corporation, as he or they may deem proper or necessary, including the institution and prosecution of any such ancillary proceedings as he or they deem advisable; [fol. 200] to settle, collect, compound, adjust or make allowances upon any debts that may be due or owing to the defendant corporation as he or they may deem proper; to pay any such claims or wages as may have priority, and in general, with all the usual powers of receivers in such cases.

3. That the officers, managers, employees, creditors, stockholders, bondholders, and noteholders, of the defendant corporation, and all other persons, firms and corporations be forthwith required to transfer, convey and deliver up to such receiver or receivers possession of all property of the defendant corporation wheresoever situated.

4. That all persons, firms and corporations be enjoined forthwith from instituting, commencing, prosecuting or continuing the prosecution of any actions, suits or proceedings at law or in equity, or under any statute, against defendant corporation, from levying or serving any attachments or executions or other processes upon the defendant corporation save and except the filing of mechanics' or other statutory liens, and generally that all persons, firms and corporations be enjoined from doing any act to interfere with said receivers in their possession of the property of the defendant corporation.

5. That your complainant may have such other and further relief as may be just or proper.

Patterson, Sherrard & Miller, Solicitors for Complainant.

Certified from the records this 22nd day of March, 1932.

J. Wood Clark, Clerk.

[fol. 201] IN THE DISTRICT COURT OF THE UNITED STATES, FOR THE WESTERN DISTRICT OF PENNSYLVANIA

No. 2554—In Equity

FRANK T. HARRINGTON, Complainant,

vs.

DUQUESNE GAS CORPORATION, Defendant.

DEFENDANT'S ANSWER TO AMENDED BILL OF COMPLAINT, ANNEXED TO PETITION OF GEORGE W. McCANDLESS

Duquesne Gas Corporation, the defendant, answers as follows the averments of the amended bill of complaint:

1. Defendant admits the averments of paragraph 1.

2. Defendant admits that complainant is the owner of 100 shares of defendant's common stock without nominal or par value. Defendant avers that complainant became the holder of record of said shares on the 21st day of September, 1931 except for the complainant's own averment that defendant has no knowledge, information, or source of information as to the date when complainant became the actual as distinguished from the record owner of said shares.

3. Answering the averments of paragraph 3, defendant [fol. 202] denies that it was organized under any statute of Pennsylvania especially applicable to public utility corporations, and avers that it was organized and now exists under and by virtue of the General Corporation Act of 1874, its amendments and supplements. Defendant avers that its business is the sale of gas to large industrial and public utility consumers under special contracts in each case, and that it does not itself sell any gas to domestic consumers. Defendant admits that Victor Gas Company, a subsidiary of the defendant, sells gas to domestic consumers, but avers that the domestic consumers to whom said Victor Gas Company sells gas do not exceed and never have exceeded the number of six. Said Victor Gas Company is a public utility corporation under the laws of Pennsylvania and is subject to regulation and control as such by the Public Service Commission of Pennsylvania. Defendant avers that a pro-

ceeding is now in progress before said Public Service Commission at Docket No. 8879 for the purpose, inter alia, of ascertaining and determining whether or not the defendant is a public utility corporation. The defendant neither admits nor denies that it is a public utility corporation, but submits the complainant's averment in that behalf to adjudication by this Court.

4. Defendant admits the averments of paragraph 4.

5. Defendant admits the averments of paragraph 5 except that defendant denies that it owns natural gas properties in West Virginia, directly or indirectly. Defendant avers that its natural gas properties in West Virginia, [fol. 203] whether held directly or indirectly through subsidiaries, are not owned in fee, but are held under lease.

6. Defendant admits the averments of paragraph 6, the said admission as to domestic consumers, however, being qualified by the averments of paragraph 3 hereof.

7. Defendant admits the averments of paragraph 7.

8. (a) Defendant admits the issuance of $4,000,000 par value of First Mortgage 6% Convertible Gold Bonds of the description alleged by complainant, that $3,965,000 thereof are outstanding, and that the interest due thereon September 15, 1931 under the terms thereof has not been paid. Defendant denies that the said bonds will mature September 15, 1945, and avers that the same are now due under the terms thereof by virtue of acceleration of maturity due to declaration of default. Defendant neither admits nor denies that it is liable on the said bonds but leaves that issue to an adjudication, hereby referring to defendant's answer in a suit in this Court entitled "Central Hanover Bank & Trust Company, as trustee under First Mortgage of Duquesne Gas Corporation dated March 15, 1930, Plaintiff, against Duquesne Gas Corporation, Defendant, No. 2577, In Equity". A copy of said answer is hereto annexed, marked Exhibit 1 and made part hereof.

(b) Defendant admits that there are now issued and outstanding $949,000 par value of Convertible 6½% Secured [fol. 204] Gold Notes of the description alleged by complainant. Defendant neither admits nor denies that it is liable thereon, but leaves that issue for adjudication by this

Court, hereby averring that the defendant's incorporation and right to do business were not submitted to or approved by the Public Service Commission of Pennsylvania, that no certificate of notification was filed with said body on the issuance of said notes, and that no action was had or taken by said commission in that behalf; and the defendant hereby refers to the averments of said Exhibit 1 in respect of the proceeding before said Commission now pending at its Docket No. 8879. Defendant admits that the interest due September 15, 1931 under the terms of said notes has not been paid.

9. Defendant admits the averments of paragraph 9.

10. Defendant denies that it is or has been doing business at a loss even without paying or providing for the interest on said bonds and notes, and avers that it is and has been doing business at a loss if the said interest be charged but at a profit if said interest be not charged; and defendant avers on information and belief that if no charge or deduction were to be made for said interest, defendant's operations would be at a profit. Defendant admits that, said interest being charged or deducted, it cannot continue to operate otherwise than at a loss unless there be a complete reorganization of the defendant in respect of its capital structure.

11. Answering paragraph 11, defendant denies that it is unable to continue to carry on its business without the [fol. 205] appointment of a receiver who can borrow funds for that purpose, and avers that the defendant now has sufficient cash resources to carry on its business and pay its current expenses. Defendant admits, however, that it cannot without greater working capital than it now has, continue to operate its business and pay, in addition to current expenses, interest upon the above mentioned bonds and notes. Defendant further admits that it cannot permanently carry on its business without reorganization and substantial changes in its capital structure. Defendant denies the complainant's averment that the defendant is presently unable to meet its due and maturing obligations, and avers that it is able to meet such obligations except the said bonds and notes and interest thereon. Defendant denies that there are any pending suits or attachments by creditors whereby the defendant's properties will be dis-

sipated, wasted and sacrificed, but admits that a suit has been commenced in this Court at No. 2577 in Equity, as aforesaid, for the principal purpose of foreclosure on said $3,965,000, face amount of First Mortgage 6% Convertible Gold Bonds. Defendant further admits that the rights, liens, priorities and securities of the holders of the defendant's said outstanding bonds, notes and stocks should be ascertained, determined, adjudicated and declared by this Court. Defendant further admits that in the opinion of the defendant this cannot be done, or the rights of all parties in interest be fairly and justly determined, or a reorganization of the defendant be effected without the interposition of this Court and the appointment of a general receiver of [fol. 206] all the defendant's properties and franchises.

12-16. Answering the averments of 12-16, both inclusive, defendant admits that said Ralph E. Davis appraised a portion of the properties now held by the defendant and that said Mattison, Davey & Winters appraised a portion thereof and that the appraisal by said Davis showed a value of the property appraised by him of $1,743,520. As to complainant's averment that the appraisal of the remainder of the properties by Mattison, Davey & Winters showed a valuation of $4,929,787, defendant avers that the aggregate of the two appraisements was $6,929,501, but that the total valuation used by the defendant's board of directors in connection with the issuance of securities was $6,673.307. Defendant did not itself employ either said Ralph E. Davis or said Mattison, Davey & Winters, and does not know what may have passed between Furlaud, Reuter & Company and said Ralph E. Davis as to the figure at which said Ralph E. Davis would have appraised the portion of defendant's properties subsequently appraised by Mattison, Davey & Winters, and does not know whether said last mentioned firm did or did not give notice to said Davis or consult with said Davis before making its appraisal. Defendant denies on information and belief that the present value of the properties now held by defendant is $3,200,000, and avers on information and belief that the present value of said properties does not exceed approximately $2,200,000. Defendant does not know and is not informed at what figure or figures said Furlaud, [fol. 207] Reuter & Company or any other person, may have disposed of the defendant's securities to the public.

17. Answering the averments of paragraph 17, defendant admits that a suit has been commenced as hereinbefore stated for the foreclosure of the above mentioned First Mortgage Bonds, and, on information and belief, that suit was brought at the instance of a Bondholders' Protective Committee other than that of which complainant is a member; but defendant avers that it is without knowledge as to the other matters alleged by complainant in said paragraph.

18. Defendant has no knowledge or information as to whether the suit described by the complainant in paragraph 18 is under contemplation or by whom as plaintiffs, or any knowledge or information in regard to any such suit other than the complainant's averments in that behalf. Otherwise, the defendant is unable to answer the averments of paragraph 18.

19. Defendant admits that said Bondholders' Protective Committee has been permitted to intervene in said proceeding now pending before the Public Service Commission of Pennsylvania. As to whether said Bondholders' Protective Committee is co-operating with said Commission or to what extent, the defendant has no knowledge or information.

20. Defendant admits the averments of paragraph 20.
[fol. 208] And for further answer, defendant avers:

21. Reference is made to said suit of foreclosure at No. 2577 in Equity, and particularly to this defendant's answer therein, being Exhibit 1 hereto attached, from which it appears that a substantial question is raised as to the validity of said $3,965,000 of First Mortgage Bonds now outstanding, and particularly as to the validity of $1,300,000 thereof. In case said First Mortgage Bonds, or any portion thereof, shall be held invalid and securities heretofore issued by the defendant subsequent in lien or security to said First Mortgage Bonds held valid, said First Mortgage Bonds or such invalid portion thereof, either would not be paid or would be subsequent in lien and security to other securities of the defendant by their terms subsequent in lien and security to said First Mortgage Bonds. So that there is inherent in the present situation a conflict, or potential conflict, in interest, between the holders or some of the holders, of the

First Mortgage Bonds and the holders of securities by their terms subsequent thereto.

22. The complainant herein avers that he is a stockholder, but in paragraph 17 of said amended bill of complaint he avers further that he is a member of a Bondholder's Protective Committee. Defendant avers on information and belief that the said committee is a committee formed in the interest of the holders of First Mortgage Bonds and that the primary interest of the complainant herein is in respect of the First Mortgage Bonds. Defendant further avers on information and belief that the complainant and the said committee of which he is a member are acting in association and co-operation with divers in- [fol. 209] vestment banking and brokerage houses by which the defendant's First Mortgage Bonds were marketed, although certain of said houses may have marketed, in addition to said First Mortgage Bonds, other securities of the defendant.

23. In said amended bill of complaint, particularly in paragraph 13 to 16 thereof, it is charged that Furlaud Reuter & Company, an investment banking house, has committed fraud upon defendant in connection with certain of the defendant's securities and is bound to make restitution.

24. Defendant avers on information and belief that said foreclosure suit at No. 2577 in Equity has been brought pursuant to demand made upon the trustee by a Bondholders' Protective Committee for holders of First Mortgage Bonds other than the Bondholders' Protective Committee of which the complainant is a member, and that said committee consists of persons connected with investment banking houses by which defendant's First Mortgage Bonds were marketed.

25. In view of the facts averred in paragraphs 22, 23 and 24 hereof, it appears that both complainants now seeking the appointment of a receiver for the defendant, to-wit, Central Hanover Bank & Trust Company as trustee at No. 2577 in Equity and the complainant in this suit, and the persons at whose instance the said complainants are acting in seeking the appointment of a receiver, are primarily interested in establishing the validity, priority, and lien of the defendant's First Mortgage Bonds as distinguished from any other class or classes of defendant's securities, where-

[fol. 210] as, as defendant submits, the ultimate solution of the defendant's present difficulties must be worked out through a general receivership, a full and impartial investigation of all the circumstances under which the defendant's securities were issued and distributed to the public, and an adjudication of the rights, liens, and priorities of all classes of security holders and creditors.

Wherefore, the defendant prays:

1. That the rights of all creditors of the defendant and of the holders of the defendant's First Mortgage Bonds, secured notes, and stock may be ascertained, decreed, and determined; that this Court will fully administer the fund in which the defendant's creditors and holders of the defendant's securities are interested, constituting all the property and assets of the defendant, in accordance with the rights, equities, liens and priorities of the creditors and stockholders of the defendant as the same finally may be ascertained and decreed by this Court.

2. That this Court, for the purpose of granting the relief prayed for herein and to protect the rights and interests of all the stockholders and creditors of the defendant, take over unto itself the jurisdiction and control of all the assets and property of the defendant of every kind and description whatsoever, and that, pending this suit, it grant such specific relief as from time to time may be expedient and appropriate to maintain such jurisdiction and control.

3. That for the purpose of preserving the unity and integrity of the property and assets of the defendant and of [fol. 211] preventing disruption thereof by any separate executions, attachments, or levies that may be attempted during the pendency of this suit, a receiver or receivers be appointed of the defendant and all of its property and assets, real, personal, and mixed, of whatsoever kind and description and wheresoever situate, and all the tolls, earnings, rents, issues, profits, revenues, and income thereof, with the usual powers of general receivers and with full power and authority to take possession of the properties, real and personal, premises, easements, franchises, leases, rights, privileges, and interests of the defendant of whatsoever kind and character, and to manage and operate the same and to continue the business of the defendant and to collect

and receive the tolls, earnings, issues, rents, profits, revenues, and income thereof, and every part thereof, and to apply the same as this Court from time to time may order and decree; and that such further powers and authority as to this Court may seem meet and proper may be granted by it to any receiver or receivers so appointed.

4. That the properties and assets and business of the defendant may be ordered to be sold as an entirety, with such exceptions and in such manner and upon such terms and conditions as this Court shall deem just and equitable, and that any such order shall make proper and suitable provisions for the protection of all just and lawful equities, rights, priorities, claims, and liens of the creditors of the defendant and shall provide for the sale of the property, assets, and business of the defendant, subject to or free and clear from any and all liens and incumbrances, and that [fol. 212] the proceeds of any such sale may be distributed by and under the direction of this Court among the creditors of the defendant adjudicated by the Court to have interests therein and such others, if any, as this Court may adjudicate to be entitled thereto.

5. That pending this suit an injunction may issue out of and under the seal of this Court enjoining and restraining all persons, including creditors of the defendant, from levying executions upon, attaching, or intermeddling with or taking possession of any of the property or assets of the defendant.

6. That the Court will make such other and further decrees and orders from time to time as may be just, meet and proper for the administration of the defendant's property and assets by the Court by its receiver or receivers and to ascertain, determine, adjudicate, protect and assure the rights of creditors of the defendant and any and all other persons having any interest, legal or equitable, in or to the property and assets of the defendant.

Duquesne Gas Corporation, By Charles C. Nuss, President. Maynard Teall, Reed, Smith, Shaw & McClay, Solicitors for the Defendant. Hause, Evans & Baker, Harrisburg, Pennsylvania, Of Counsel.

(Verified by Charles C. Nuss, President, Jan. 15, 1932.)

[fol. 213] CERTIFIED COPY OF RESOLUTION OF BOARD OF DIRECTORS OF DUQUESNE GAS CORPORATION, ANNEXED TO ANSWER IN HARRINGTON v. DUQUESNE GAS CORPORATION

Whereas, in the District Court of the United States for the Western District of Pennsylvania, at No. 2554 in Equity, Frank T. Harrington, as complainant, has filed suit against this corporation for a receiver and for relief as prayed for in his bill of complaint, an answer having been filed thereto by C. C. Nuss, President of the corporation; and

Whereas, on January 12, 1932 an amended bill of complaint was filed by the complainant in said cause, to which no answer on the part of this corporation has as yet been filed; and

Whereas in the said Court at No. 2577 in Equity, Central Hanover Bank & Trust Company, as trustee under the First Mortgage Indenture, has filed bill of complaint for foreclosure and other relief to which answer has been filed by this corporation through the agency of C. C. Nuss as President; and

Whereas in connection with said last mentioned proceeding, formal application has been made to the Court for the appointment of a receiver; and

Whereas the said suits and the status of the company with respect to its outstanding securities present a very complicated situation on which it is necessary for the President of the company to keep in close touch with counsel and [fol. 214] possibly to take such action as his judgment may commend without previous authorization of this board as to each specific action proposed to be taken by the corporation.

Resolved, that C. C. Nuss, the President of this corporation, be, and hereby is, authorized and empowered after consultation with counsel, to take such action on behalf of this corporation as his judgment may commend in connection with either of the before mentioned suits or any other suits entered by or against this corporation arising in connection with its outstanding securities or any of the same or its obligations with respect thereto.

Resolved, further, that C. C. Nuss, the President of this corporation, be, and hereby is, authorized in his discretion, and on behalf of this corporation, to consent to the appointment of a receiver for this corporation in either of the above

mentioned suits or any other suit; provided that the said C. C. Nuss shall first consult with counsel in regard thereto.

[fol. 215] STATE OF PENNSYLVANIA,
County of Alleghany, ss:

I, Harry J. Steele, Secretary of Duquesne Gas Corporation, hereby certify that the foregoing is a true and correct copy of preambles and resolutions adopted by the Board of Directors of this corporation at a meeting duly held on January 15, 1932.

Harry J. Steele, Secretary. (Corp. Seal.)

Sworn to and subscribed before me this 15th day of January, A. D. 1932.

Fern F. Mesing, Notary Public. (Notarial Seal.)

Certified from the record this 22nd day of March, 1932.

J. Wood Clark, Clerk.

[fol. 216] IN THE DISTRICT COURT OF THE UNITED STATES, FOR THE WESTERN DISTRICT OF PENNSYLVANIA

In Equity No. 2577

CENTRAL HANOVER BANK & TRUST COMPANY, as Trustee under First Mortgage of Duquesne Gas Corporation dated March 15, 1930, Plaintiff,

against

DUQUESNE GAS CORPORATION, Defendant

EXHIBIT I, ANNEXED TO ANSWER OF DUQUESNE GAS CORPORATION

Duquesne Gas Corporation, the defendant herein, admits the averments of the Bill of Complaint made in paragraphs First to Fifteenth (both inclusive) thereof, except it does not admit (1) that it, the said defendant, is a corporation duly organized and existing under the laws of Pennsylvania, or (2) that all said $3,965,000.00 of First Mortgage Bonds now outstanding are in the hands of bona fide holders thereof for value, or (3) that all said $3,965,000.00 of bonds now outstanding, and particularly $1,300,000.00 par value thereof, are the lawfully issued, valid, and binding obliga-

tions of the defendant, or (4) that the said mortgage creates and establishes the first lien it purports to create and establish; but the defendant leaves the said not admitted matters [fol. 217] for determination and adjudication upon the facts hereinafter stated:

Sixteenth: The defendant corporation was organized and created under the Act of Assembly of the Commonwealth of Pennsylvania of April 29, 1874, P. L. 73, and its amendments and supplements, with charter powers as follows:

"Said corporation is formed for the purpose of mining, drilling, boring for and producing petroleum, oil, natural gas and other minerals and substances, incidentally developed, and the manufacturing, buying, selling, trading and dealing in the products and by-products thereof; the acquiring and holding of such lands, lease., mining and drilling rights, and the construction, erection and operation of such lines, pipe lines, buildings, machinery and appliances as may be necessary and convenient therefor and the transaction of all such business as is necessary and incidental thereto."

Seventeenth: At the time of organization and issuance of its securities, including the said First Mortgage Bonds, the defendant was advised by counsel that it was not a public service company or subject to the Public Service Company Law of Pennsylvania (Act of July 26, 1913, P. L. 1374); accordingly, the defendant did not seek or obtain the approval of said Public Service Commission to be incorporated, organized, or created, or to begin the exercise of any right, power, franchise or privilege and did not on or prior [fol. 218] to the date it issued its securities, including said First Mortgage Bonds, file with said Commission its certificates of notification covering the issuance of said securities, or with respect to either of said matters, take any proceeding before said Commission.

Eighteenth: On April 28, 1931, the said Public Service Commission, purporting to act under said Public Service Company Law, issued its order at Complaint Docket No. 8879 against this defendant as follows:

"That an inquiry and investigation upon the Commission's own motion be and is hereby instituted into the status of the Duquesne Gas Corporation, and its failure to comply

with the provisions of the laws of the Commonwealth applicable to public service companies; said inquiry to be scheduled for hearing and/or argument if desired not less than fifteen (15) days from the date of service hereof upon notice."

Said order was duly served upon the defendant, and a certified copy thereof is attached hereto, marked Exhibit "A", and made part hereof.

On September 1, 1931, said Commission, at the same docket number, issued a further order against defendant as follows:

"That the inquiry and investigation heretofore instituted by the Commission on its own motion under date of April 28, 1931, be and is hereby extended to include an inquiry and [fol. 219] investigation into the promotion, organization, financing and acquisition of the properties of the Duquesne Gas Corporation, and its failure to comply with the provisions of the laws of the Commonwealth applicable to public service companies."

Said further order was duly served on this defendant, and a certified copy thereof is hereto attached, marked Exhibit "B", and made part hereof.

On November 24, 1931, at the same docket number, a further order was made in said proceeding as follows:

"That S. P. Woodward, Frank T. Harrington, C. E. Wheeler and V. Blake Allison, constituting a Bondholders' Protective Committee of Duquesne Gas Corporation be and are hereby permitted to intervene in said complaint."

Said last mentioned order was duly served on this defendant, and the same is annexed hereto, marked Exhibit "C", and made part hereof.

Nineteenth: Said Commission has not as yet terminated said proceeding at its Docket No. 8879 or made any determination as to the sufficiency of this defendant's organization as a corporation or as to the validity of any of this defendant's outstanding securities or of the issuance thereof, but the said proceeding at Docket No. 8879 is still pending before said Commission and undetermined.

[fol. 220] The defendant avers the following facts in respect of, particularly, the above mentioned $1,300,000 par value of said First Mortgage Bonds:

Twentieth: The defendant corporation was organized on or about February 13, 1930, with authorized capital stock of 1,000 shares without nominal or par value having a stated capital of $500.00, which latter amount was paid in cash. On March 5, 1930, the defendant's organization meeting having been held February 21, 1930, the Board of Directors of the defendant authorized an increase of capital stock from 1,000 shares as aforesaid to 1,250,000 shares without nominal or par value having a stated capital of $625,000.00 and also authorized an increase of indebtedness from nothing to $10,000,000.00, and called a special meeting of stockholders for April 3, 1930, for the purpose, inter alia, of considering and acting upon the said increases of capital stock and indebtedness.

Twenty-first: Said meeting of stockholders was held on said appointed day, April 3, 1930, and said increases of capital stock and indebtedness were authorized and approved by the stockholders; the stockholders waived preemptive rights on the new stock so authorized; an amendment to the by-laws was approved providing that the stockholders should not have pre-emptive rights on new stock; the directors were authorized to issue stock up to 1,250,000 shares for such consideration as they should approve; the directors were authorized to accept an offer of Furlaud & Company, Inc., a New York corporation, to buy 139,000 shares of the just authorized stock for fifty cents per share, [fol. 221] or $69,500.00; engineers' and accountants' reports were submitted on the properties intended to be acquired by the company; the indenture under which said First Mortgage Bonds were issued was approved; a General Mortgage Indenture was approved under which $1,000,000.00 of General Mortgage 6½% Gold Bonds might be issued; and an agreement was approved under which Secured Gold Notes might be issued to the amount of $1,000,000.00 secured by $1,000,000.00 of said General Mortgage 6½% Gold Bonds.

Twenty-second: On April 7, 1930, a special meeting of the Board of Directors of the defendant corporation was held at which the following business was transacted: (1) Said offer of Furlaud & Company, Inc., to buy 139,000

shares of stock for $69,500.00 was accepted; (2) execution and delivery of the above mentioned indentures and agreement were authorized; (3) 400,000 shares of stock were set apart to meet the conversion requirements of the First Mortgage Bonds and Secured Notes; (4) a proposed agreement between Kingston Corporation (a New Jersey corporation) and the defendant was authorized and approved under which the defendant was to acquire its properties, the substance of said agreement being as follows:

(a) Kingston Corporation to transfer the said properties to the defendant corporation;

(b) The defendant corporation to pay the Kingston Corporation therefor by discharging $3,015,000.00 of indebted-
[fol. 222] ness owing by Kingston Corporation to Central Hanover Bank & Trust Company, the complainant herein, and by delivering to said Kingston Corporation $1,300,-000.00 par value of this defendant's First Mortgage Bonds and 535,000 shares of this defendant's stock:

(5) an offer of said Furlaud & Company, Inc., to buy $2,700,000 par value of said First Mortgage Bonds at $900.00 and accrued interest per bond and $1,000,000.00 par value of said Secured Notes at $880.00 and accrued interest per note was accepted.

Twenty-third: Shortly after the said meeting the Kingston Corporation transferred said properties to the defendant corporation and the defendant corporation paid therefor as agreed; and said $2,700,000.00 of First Mortgage Bonds were delivered to Furlaud & Company, Inc., for $900.00 per Bond in cash and $1,000,000.00 of said Secured Notes were delivered to said Furlaud & Company, Inc., for $880.00 per note in cash, with accrued interest in each case.

Twenty-fourth: The defendant avers on information and belief that said Kingston Corporation was a subsidiary of said Furlaud & Company, Inc., and in said transaction was subject to the control of and in fact was controlled by said Furlaud & Company, Inc. Defendant further alleges, also upon information and belief, that the said properties transferred to the defendant corporation for, in effect, $3,015,-000.00 in cash, $1,300,000.00 of First Mortgage Bonds, and
[fol. 223] 535,000 shares of stock had cost the said King-

ston Corporation, for the properties and all expenses in connection with the acquirement thereof, only $3,015,000.00.

Twenty-fifth: Defendant alleges on information and belief that at the time and times of all the directors' and stockholders' meetings hereinbefore referred to, said Furlaud & Company, Inc., owned all the stock of the defendant then outstanding except directors' qualifying shares, and the defendant's directors were the nominees of and were under the control of and in fact were controlled by said Furlaud & Company, Inc., and said Furlaud & Company, Inc., was the promoter of the defendant corporation and its organization and of the sale of the defendant's First Mortgage Bonds and other securities.

Twenty-sixth: On April 7, 1930, subsequent to the meeting of the Board of Directors of the defendant corporation above referred to and held on the same day, the then directors of the defendant corporation, three in number, resigned, and the number of the Board of Directors of the defendant was increased to six, and six new directors, and also a new President and a new treasurer, were elected.

Twenty-seventh: When the said transaction between the defendant corporation and Kingston Corporation was authorized and approved as above stated, the stockholders and directors of the defendant had before them reports of engineers of high standing showing the gas reserves and plant [fol. 224] and equipment to have a value of $6,923,501.00 based upon a certain program of development; but in said reports the gas reserves of non-operating properties held merely under lease were included in the valuation on a gas reserve basis, whereas, for the issuance of bonds thereon which was made subsequent to said reports, the said non-operating properties, as defendant alleges on information and belief, should have been placed on a value-of-acreage basis. The defendant avers on information and belief that on a value-of-acreage basis for non-operating properties held under lease the properties acquired by the defendant corporation from Kingston Corporation did not have a value in excess of $3,015,000.00, which was the amount, or the approximate amount including expenses, paid therefor by said Kingston Corporation.

Twenty-eighth: In view of the facts hereinabove stated, the defendant does not know, and therefore leaves to ju-

dicial determination, whether said $1,300,000.00 of First Mortgage Bonds delivered to Kingston Corporation in connection with the acquirement of the defendant's properties did or did not constitute a fictitious issue of securities for which the issuer received no value.

Twenty-ninth: Defendant does not know who are the persons now holding said $1,300,000.00 of bonds delivered to said Kingston Corporation, or whether the holders thereof acquired the same for value or with or without notice of the matters hereinbefore averred, or whether said $1,300,000.00 of bonds are valid obligations of the defendant cor-
[fol. 225] poration or entitled to the lien and security of the said First Mortgage Indenture.

Duquesne Gas Corporation, by C. C. Nuss, President.

Maynard Teall, Reed, Smith, Shaw & McClay, Solicitors for Defendant. Hause, Evans & Baker, Harrisburg, Pennsylvania, of Counsel.

(Verified by C. C. Nuss on December 7, 1931.)

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DISTRICT OF PENNSYLVANIA

No. 2554. In Equity

FRANK T. HARRINGTON, Plaintiff,

vs.

DUQUESNE GAS CORPORATION, Defendant

PER CURIAM DECREE, ANNEXED TO PETITION OF GEORGE W. McCANDLESS

And now, to-wit, January 19, 1932, the above cause came on for further hearing upon the bill of complaint as amended and the answer of the respondent as amended, [fol. 226] and it appearing to this Court that another action, brought by the Central Hanover Bank and Trust Company as Trustee under the first mortgage of the Duquesne Gas Corporation dated as of March 15, 1930, against said Duquesne Gas Corporation at No. 2577 in Equity, seeks the foreclosure of the said first mortgage on the properties of

the above named defendant, and that a complaint and answer have been filed therein, and the plaintiff in this action, No. 2554 in Equity, appearing by his solicitor, Clark Miller, Esq., and the defendant, by its solicitor, Maynard Teall, Esq., and the plaintiff in the proceeding at No. 2577 in Equity appearing by its counsel, Frank B. Ingersoll, Esq., and the defendant in said action by its counsel, Maynard Teall, Esq., and all of said counsel consenting to the entry of this order and the Court being fully advised of the premises, it is now

Ordered, adjudged and decreed:

1. That George W. McCandless, of the City of Pittsburgh, Pennsylvania, be and he is hereby appointed receiver of all and singular the assets, lands, tenements and hereditaments of the defendant, the Duquesne Gas Corporation, and all of its property, real, personal and mixed, of every nature and kind whatsoever, including all pipe lines, machinery, appliances, fittings and equipment belonging to or connected therewith, and all oil and gas rights, leases and leaseholds and the wells, derricks, drain pipes, casing, tubing, machinery and appliances and equipment thereon, connected therewith or belonging thereto, and all leases, contracts, stocks, bonds, obligations, choses in action, ac- [fol. 227] counts and rights owned by, belonging to or due to the defendant company, and all rights, franchises, income and profits granted to, acquired by or belonging to the defendant company.

2. That said receiver shall, before entering upon his duties hereunder, give and file with the Court a bond in the penal sum of $50,000 with surety or sureties approved by this Court, and conditioned that he will faithfully perform his duty as receiver herein and in any ancillary proceedings wherein he may be appointed, and will well and truly account for any and all moneys or property coming into his hands as such receiver, in accordance with the provisions of this order or any other order which may from time to time be issued by this Court, and abide by and perform all things which he is herein or may hereafter be directed to perform in this cause or in any ancillary proceedings wherein he is appointed.

3. Upon the filing and approval of the said bond, said receiver be and he is hereby authorized, empowered and

directed to take immediate possession of all and singular the assets above described or referred to, wherever the same may be situate or found, and, until a further order of this Court, to continue the operation of the business of the defendant company and every part or portion thereof and to run, manage and conduct such business under leases, contracts or arrangements as heretofore run, managed, conducted and operated by the defendant company, but the Court expressly reserves to itself the right to pass upon, disapprove, disavow and cancel any and all leases, arrangements and contracts of every nature, kind and de-
[fol. 228] scription under or by virtue of which the defendant company has been or is now operating any of its property.

The receiver shall exercise all such powers as are usually exercised by receivers and all such as are necessary, useful or convenient to the proper conduct by him of the business of the corporation, and he shall discharge all such duties as are within the line, scope and purpose of his appointment, including full power and authority to demand, sue for, collect, receive and take into possession the goods, chattels, rights, credits, moneys, effects, books and property of every description belonging to said defendant, Duquesne Gas Corporation, and including power to do any and all other acts which may be necessary to preserve the rights and properties of said defendant, Duquesne Gas Corporation. The receiver shall also exercise such further powers as the Court may from time to time grant.

4. That the defendant corporation and each and every of its officers, directors, agents and employees and all other persons, associations and corporations are now and hereby ordered, commanded and directed to turn over and deliver to such receiver, or his duly constituted representatives, any and all of the books of account, records, vouchers, checks, deeds, leases, contracts, agreements, notes, accounts, moneys, stocks, bonds, obligations and property of every kind and nature, real, personal and mixed, now in or which may hereafter come into his or their hands, control or possession.

That the defendant corporation and each and every of
[fol. 229] its said officers, directors, agents and employees and all other persons, associations and corporations be and they are now and hereby restrained and enjoined during

the pendency of this cause and the administration of the said receiver from transferring, selling, disposing of, or interfering with any of the property of the defendant corporation and from taking possession of or in any way interfering with the same or any part thereof, and from disturbing, preventing, or in any way interfering with the receiver in his possession, control, operation or management of the property, or any part thereof, of the defendant company over which the said receiver is hereby appointed as such; and from instituting, commencing, prosecuting or continuing the prosecution of, except as herein provided, any actions, suits or proceedings at law or in equity against the defendant corporation, from levying or serving any attachments or executions or other processes upon the defendant corporation save and except the filing of mechanics' or other statutory liens and save also as herein provided; and from disturbing, preventing or in any way interfering with the receiver in the discharge of his duties hereunder.

5. As soon as may be after the entry of this order, the receiver shall segregate and sequester for the benefit of the Trustee, plaintiff, at No. 2577 in Equity, and the holders of the first mortgage bonds of the defendant and appurtenant coupons secured by the first mortgage, all income, rents, issues and profits from the property, subject to the lien of the first mortgage, and apply the same to and for their benefit, subject only to such expenses and other uses [fol. 230] as may be legally and properly incurred in the operation and preservation of said property, having due regard to the rights of the said bondholders and the Trustee, plaintiff, at No. 2557 in Equity, and to the protection of the security of the first mortgage.

The receiver, as soon as practical and convenient, shall cause to be prepared a schedule of all and singular the property of the defendant, subject to the lien of the first mortgage, which may come into his possession as such receiver, and shall file the same with the Clerk of this Court, and he is directed to keep separate accounts of his transactions as such receiver and of such moneys and other property and assets which may from time to time come into his hands as such receiver, and of the rents, issues, and profits of the property and assets, subject to the lien of the first mortgage, and to make report thereof from time to time as this Court may direct, but said schedule, account and/or reports

shall not be conclusive on the Trustee, plaintiff, in the action at No. 2577 in Equity, it being further provided that said segregation and sequestration and separate accounting shall be without prejudice to any rights of the parties in said action at No. 2577 in Equity and shall not be taken as any adjudication of the rights of the first mortgage bondholders or any other class of security holders.

6. This action and that at No. 2577 in Equity, in which the Central Hanover Bank and Trust Company, as Trustee, is plaintiff, and the Duquesne Gas Corporation is defendant, be and the same are hereby consolidated and that action and all the proceedings therein shall hereafter be brought and [fol. 231] docketed under the title, number and term of this action, said consolidation being made without prejudice to the rights of the parties as accrued under the pleadings heretofore filed in said action at No. 2577 in Equity.

7. The Court reserves the full right and jurisdiction from time to time to make such further orders or decrees amplifying, extending, limiting or otherwise modifying this order as to it may at any time seem proper and in all respects and at all times to regulate and control the conduct of the receiver.

Per Curiam.

S.

Certified from the record this 22nd day of March, 1932.
J. Wood Clark, Clerk.

District Court of the United States, Western District of Pennsylvania

No. 2554 in Equity

Frank T. Harrington, Complainant,

vs.

Duquesne Gas Corporation, Defendant

Certificate, Annexed to Petition of George W. McCandless

I, J. Wood Clark, Clerk of the United States District Court for the Western District of Pennsylvania do hereby

certify that bond in the sum of $50,000 filed by George W. [fol. 232] McCandless, Receiver, was filed and approved by the Court on the 20th day of January, 1932.

Witness my hand and the seal of this Court this 22nd day of March, 1932.

J. Wood Clark, Clerk. (Seal of the United States District Court, Western District of Pennsylvania)

UNITED STATES DISTRICT COURT, FOR THE SOUTHERN DISTRICT OF NEW YORK

In Equity No. 66-184

FRANK T. HARRINGTON, Complainant,

against

DUQUESNE GAS CORPORATION, Defendant

ORDER APPOINTING GEORGE W. MCCANDLESS ANCILLARY RECEIVER, ANNEXED TO PETITION OF GEORGE W. MCCANDLESS

Upon the annexed bill of complaint filed in the above entitled suit in the United States District Court for the Western District of Pennsylvania, and upon the answer of the defendant therein to said amended bill of complaint, and upon the per curiam decree therein of the United [fol. 233] States District Court for the Western District of Pennsylvania, dated the 19th day of January, 1932, appointing George W. McCandless receiver of the assets, lands, tenements and hereditaments of the defendant Duquesne Gas Corporation, and all of its property real and personal, including choses in action, and upon the certificate of the Clerk of the United States District Court for the Western District of Pennsylvania of the filing and the approving of the bond of said receiver, and upon reading and filing the petition of said George W. McCandless, duly verified the 23 day of March, 1932 from which it appears to the satisfaction of the Court that there is need of an ancillary receivership in this district.

Now, on motion of Ehrich, Royall, Wheeler & Walter, solicitors for the petitioner, it is

Ordered, adjudged and decreed that George W. McCandless be and he hereby is appointed ancillary receiver of

Duquesne Gas Corporation in and for the Southern District of New York to carry into force and effect the order of the Court of original jurisdiction, and it is further

Ordered, adjudged and decreed that said ancillary receiver is hereby authorized to bring an action against the promoters of said corporation, including Maxime H. Furlaud and Carlos Reuter, for an accounting and for the restitution of funds fraudulently diverted and misappropriated and of secret and excessive profits; and to petition for an order to retain solicitors for that purpose; and to do any and all things necessary to be done in connection therewith; and it is further

[fol. 234] Ordered, adjudged and decreed that the defendant, its agents or employees, stockholders, creditors and all marshalls, sheriffs, constables and all other officers, and generally all persons, firms and corporations whatsoever, are hereby enjoined from interfering or attempting to interfere in any manner with said ancillary receiver in effecting such purposes, and it is further

Ordered, adjudged and decreed that before entering upon the performance of any of his duties the said ancillary receiver shall execute and file with the Clerk of this Court a bond with one or more sureties approved by this Court in the penal sum of Twenty-five thousand Dollars ($25,000) conditioned upon the faithful discharge of his duties, and that upon any moneys or funds coming into his hands said ancillary receiver shall immediately report the fact to the Court and submit to the Court the question of an increase of this bond, and it is further

Ordered, adjudged and decreed that any corporate surety duly qualified in accordance with General Rule 28 of this Court shall be sufficient for this purpose, and it is further

Ordered, adjudged and decreed that said ancillary receiver shall make himself amenable to the jurisdiction of this Court and shall authorize his attorneys within this District to accept upon his behalf service of any process of the Federal and State Courts within this District and shall have leave to apply to this Court for further orders and authority and shall comply with all orders of the Court of original jurisdiction.

(Signed) Wm. Bondy, U. S. D. J.

March 23, 1932.

[fol. 235] PLAINTIFF'S EXHIBIT 2

This Agreement made and entered into this 5th day of February 1930, by and between Kingston Corporation, a New Jersey Corporation (hereinafter sometimes called the "Purchaser"), party of the first part, and J. B. Nuss and Anna Nuss, his wife, and C. C. Nuss and Ada C. Nuss, his wife, (hereinafter sometimes called the "Vendor"), party of the second part: Witnesseth:

First: The Vendor represents that he is in a position to cause the leases, leaseholds, gas sale contracts, and equipment listed respectively in Schedules A, B and C attached hereto, to be conveyed to Purchaser, or his nominee, in accordance with the provisions hereof.

Second: Vendor agrees to sell and Purchaser agrees to purchase the property described in paragraph "First" hereof for the sum of Six hundred sixty thousand ($660,000) Dollars cash, subject, however, to the provisions of paragraph "Fifth" hereof.

Third: Vendor agrees to deliver to Purchaser on the day of payment hereinafter provided, valid bargain and sale deeds, bills of sale, and/or assignments conveying, transferring and assigning as good a title to all the property referred to in paragraph "First" hereof and more specifically described in Schedules A, B and C attached hereto, as the owner thereof now has, to Purchaser or his nominee, and as to all operated leaseholds, free from obligations, liens and encumbrances except only current taxes not in de-
[fol. 236] fault, and subject to such limitations as may be set forth in any of the above recited leases and/or the above described gas sales contracts.

Fourth: Purchaser, subject to the terms and provisions of this agreement, hereby agrees to pay for the property, the subject of this agreement, and Vendor agrees to deliver to Purchaser the deeds and/or assignments described in paragraph "Third" hereof at the principal office of Furlaud & Company, Inc., (or at such other place as Purchaser may elect and of which election Purchaser shall give Vendor ten days' notice, either by letter or telegram to Vendor at Washington, Pennsylvania), on the 25th day of March, 1930, or at such date prior thereto as Purchaser

shall elect and of which prior date, if such election shall be made, Purchaser shall give Vendor notice similarly as above specified with respect to any change of place of payment. The time of payment of the purchase price and delivery of said deeds and/or assignments, whether on March 25th, 1930, or on a date prior thereto as in this paragraph provided, is hereby defined to be the date of final payment thereunder.

Fifth: Vendor agrees that Purchaser shall have until March 25th, 1930, to make an examination of the property, papers, books, records, evidences of title and other documents of Vendor and it is further agreed that if such examination should disclose any condition which, in the judgment of the Purchaser, his engineers, auditors, and/or counsel, or if any other condition should exist, which in the judgment of the Purchaser would render it inadvisable to carry out this agreement, then, in such event and upon [fol. 237] notice thereof to Vendor at Washington, Pennsylvania, either by telegram or in writing, on or prior to March 15th, 1930, all liability of the parties hereunder shall terminate. In the event, however, that Purchaser shall notify Vendor at the above mentioned address, by letter or telegram, on or prior to March 15th, 1930, that the examination of the property referred to in paragraph "First" has been satisfactorily completed and that he elects to proceed hereunder, then the time for payment hereunder shall be extended to such date within ten days after the date on which such notice is sent as the Purchaser shall specify in such notice, provided the Vendor shall be given at least five days in which to cause to be prepared, executed and delivered all instruments necessary on his part to carry out this agreement.

Sixth: It is mutually understood and agreed that regardless of the date on which final payment may be made hereunder the properties referred to in paragraph "First" hereof shall be deemed to have been acquired on February 1, 1930, and that in the event the Purchaser or his nominee elects to proceed hereunder and acquire such property he shall receive all of the income accruing to such property from February 1, 1930, to the date of final payment, less such amount as may have actually been expended in connection with the operation of such property, and the Pur-

chaser, if he elects to proceed hereunder, shall pay to the Vendor interest at the rate of six per cent on the total purchase price specified in paragraph "Second" hereof from February 1, 1930, to the date of final payment. At the time of final payment the parties hereto will make such adjustment of the net income as is then possible but in the event [fol. 238] complete reports from the operation of the property referred to in paragraph "First" hereof are not available at the time of final payment, then adjustment shall be made during the ensuing period of sixty days after the date of final payment during which time it is expected that complete data will be available.

Seventh: The Vendor agrees:

(a) That from the date hereof until the time of final payment he will cause the property referred to in paragraph "First" hereof and all wells situated upon the properties included therein to be operated in a prudent manner and with the care usually bestowed by operators of similar properties.

(b) That from and after the date hereof until the date of final payment he will permit no agreement to be entered into for the sale of gas, oil and other by-products produced from the leases described in Schedule "A" and will permit no other contract involving any of the property referred to in paragraph "First" hereof to be entered into which extends beyond the date of final payment without the written consent of the Purchaser.

(c) That the Purchaser may assign this contract to any person, firm and/or corporation which he shall elect and upon such assignment all rights and liabilities of the Purchaser hereunder shall inure to the benefit of and be binding upon such assignee.

(d) That in connection with his causing the transfer of the property referred to in paragraph "First" hereof to the Purchaser and/or his nominee, he will cause all steps to [fol. 239] be disclosed to the Purchaser and his counsel and will submit all documents incident thereto for the approval of such counsel to the Purchaser. Further that he will cause to be executed and delivered any and all documents which counsel to the Purchaser may reasonably request in

order to carry out the conveyance, transfer and assignment of all the property referred to in paragraph "First" hereof.

(e) That he will hold the Purchaser and his assignees harmless from any and all claims of the government of the United States of America and/or of the Commonwealth of Pennsylvania for any taxes which may have accrued prior to January 1, 1930, to either of such governmental bodies or to any political subdivision of the Commonwealth of Pennsylvania and be chargeable against any part of the property referred to in paragraph "First" hereof, and against any and all liability arising out of the proposed transfer of all of the property referred to in paragraph "First" hereof to the Purchaser and/or his assigns.

Witness the following signatures and seals the day and year first above written.

Kingston Corporation, by Otto E. Schuller, Vice President.

Attest: —— ——.
Asst. Secy.

Witness:
H. M. Thompson, J. B. Nuss, (Seal).
Lucy Stewart, Anna Nuss, (Seal).
H. M. Thompson, C. C. Nuss, (Seal).
Lucy Stewart, Ada C. Nuss, (Seal).

Annexed to Plaintiff's Exhibit No. 2 are Schedules A, B and C containing a detailed statement of the leases, lease-[fol. 240] holds, gas sale contracts and equipment to be conveyed to the purchaser or his nominee under the terms of the contract set forth in Plaintiff's Exhibit No. 2.

PLAINTIFF'S EXHIBIT 3

Agreement entered into the 7th day of January, 1930, by and between Daniel Ritter, as Purchaser, and t[illegible] Henderson Oil & Gas Co. as Vendor, providing for a purchase price of $165,000 for certain properties.

Annexed to this agreement appears the following assignment:

"In consideration of the sum of One dollar ($1.00) to me in hand paid and for other good and valuable con-

siderations, receipt of which is hereby acknowledged, I hereby sell, assign, transfer and set over unto Kingston Corporation, a corporation organized and existing under and by virtue of the laws of the State of New Jersey and duly authorized to transact business in the Commonwealth of Pennsylvania, its successors and assigns, all my right, title and interest in and to the attached contract between Daniel Ritter of Wynnewood, Pa., and Henderson Oil & Gas Company of Breckenridge, Pa., dated the 7th day of January, 1930.

Daniel Ritter (L. S.) Kingston Corporation (L. S.)
by Carlos Reuter, V. P.

Witness James F. Sullivan.
Witness R. Halporn."

Plaintiff's Exhibit No. 3 is otherwise similar in form and in content to Plaintiff's Exhibit No. 2.

[fol. 241] PLAINTIFF'S EXHIBIT 4

This exhibit is an agreement dated the 27th day of December, 1929, entered into by and between the defendant Kingston Corporation, as Purchaser, and A. Q. Starr, L. F. Carson and H. T. Wynn, as Vendors, affecting the property known as the Trafford Oil & Gas Co. properties, and providing for a purchase price of $815,000, which agreement was signed by M. H. Furlaud as President of Kingston Corporation.

Plaintiff's Exhibit No. 4 is otherwise similar in form and content to Plaintiff's Exhibit No. 2.

PLAINTIFF'S EXHIBIT 5

This exhibit is an agreement made and entered into on the 6th day of January, 1930, between Daniel Ritter, as Purchaser, and P. L. Wally, as Vendor, covering the Wally property, and providing for a purchase price of $135,000.

Attached to this agreement is an assignment executed by Daniel Ritter to Kingston Corporation, similar to the assignment set forth in Plaintiff's Exhibit No. 3. Said as-

signment was executed by Kingston Corporation, by Carlos Reuter, Vice-President, and R. Halporn, as witness. Otherwise, the agreement in form and content is similar to the agreement set forth in Plaintiff's Exhibit No. 2.

[fol. 242] PLAINTIFF'S EXHIBIT 6

This exhibit consists of two agreements dated February 5, 1930, the first entered into by Kingston Corporation, as Purchaser, and Victor D. Behm and Mary E. Behm, his wife, as Vendors, and the second entered into on the 5th day of February, 1930, by Kingston Corporation as Purchaser, and Victor Behm as Vendor, and providing for an aggregate purchase price of $200,000 for the Behm properties. Said agreement was signed by Otto E. Schuller as Vice-President of Kingston Corporation.

Both of said agreements are in form and in content similar to Plaintiff's Exhibit No. 2, and cover the properties known as the "Behm Properties".

PLAINTIFF'S EXHIBIT 7

This exhibit consists of an agreement entered into on the 2nd day of January, 1930, between Daniel Ritter as Purchaser, and I. T. Campbell, as Vendor, covering the property known as the "Campbell Property", and providing for a purchase price of $135,000.

Attached to this agreement is an assignment by Ritter to Kingston Corporation in form similar to that appearing in Plaintiff's Exhibit No. 3.

The agreement, otherwise, is in form similar to Plaintiff's Exhibit No. 2.

PLAINTIFF'S EXHIBIT 8

This exhibit consists of an agreement dated February 5, 1930, between Kingston Corporation as Purchaser, and C. V. Garrison and Raymond Orrill, as Vendors, covering [fol. 243] the property known as the "Garrison Property", and providing for a purchase price of $120,000. Said

agreement was signed by Otto E. Schuller as Vice-President of Kingston Corporation.

This exhibit is in form similar to Plaintiff's Exhibit No. 2.

PLAINTIFF'S EXHIBIT 9

This consists of an agreement dated the 4th day of January, 1930, between Daniel Ritter, as Purchaser, and A. J. Degenther, as Vendor, covering the property known as the "Byers Property", and providing for a purchase price of $125,000.

Attached to the agreement is an assignment to Kingston Corporation executed by Daniel Ritter. Said assignment was signed by Kingston Corporation, by Carlos Reuter. The said assignment is in form similar to assignment appearing in Plaintiff's Exhibit No. 3.

Otherwise, the agreement is in form similar to that appearing in Plaintiff's Exhibit No. 2.

PLAINTIFF'S EXHIBIT 10

This consists of an agreement dated the 8th day of January, 1930, between Daniel Ritter as Purchaser, and James S. Gallagher, as Vendor, covering the Gallagher Property, and providing for a purchase price of $185,000.

Attached to this agreement is an assignment to Kingston Corporation executed by Daniel Ritter. Said assignment was executed by Kingston Corporation, by Carlos Reuter, Vice-President, and witnessed by R. Halporn. The assignment is in form similar to that appearing in Plaintiff's Exhibit No. 3, and the agreement is otherwise similar in form and in content to that appearing in Plaintiff's Exhibit No. 2.

(Here follows table, side folio 244.)

[fol. 244]

Plaintiff's Exhibit 11

Schedule Showing Purchase Price of Properties Between Owners of Gas Properties and Kingston Corporation

Group	Name of property	Sales agreement Date	Sales agreement Name	Assignment of sales agreement Date	Assignment of sales agreement Name	Purchase price per agreement	To secure extension	Payments Under escrow agreement	Payments Final settlement per working papers of Barrow, Wade Guthrie & Co.	Total
1.	Henderson Oil & Gas Co	1- 7-30	Daniel Ritter	1- 7-30	Kingston Corp.	165,000.00	5,000.00	157,000.00	3,000.00	165,000.00
	James S. Gallagher	1- 8-30	Daniel Ritter	1- 8-30	Kingston Corp.	185,000.00	2,000.00	178,000.00	5,000.00	185,000.00
2.	Trafford Oil and Gas Co		Daniel Ritter		Kingston Corp.	815,000.00	10,000.00	790,000.00	15,000.00	815,000.00
	I. T. Campbell	1-29-30	Daniel Ritter	1-29-30	Kingston Corp.	125,000.00	3,000.00	117,900.00	4,100.00	125,000.00
3.	P. L. Wally	1- 6-30	Daniel Ritter	1- 6-30	Kingston Corp.	135,000.00	1,500.00	125,000.00	8,500.00	135,000.00
	A. J. Degenther	1- 4-30	Daniel Ritter	1- 4-30	Kingston Corp.	125,000.00	1,500.00			
	Byers Property							128,500.00	9,000.00	139,000.00
	A. J. Degenther—1 Well	2- 4-30	Daniel Ritter	2- 4-30	Kingston Corp.	14,000.00				
4.	C. C. Nuss, et al	2- 5-30	Kingston Corp.			660,000.00	13,000.00	647,000.00		660,000.00
	W. G. Wade—Acreage	1-28-30	C. C. Nuss	1-30-30	Kingston Corp.	5,135.00	500.00	4,635.00		5,135.00
5.	Victor D. Behm, et ux	2- 5-30	Kingston Corp.			187,500.00	4,000.00			
	Victor D. Behm							190,000.00	6,000.00	200,000.00
	Victor Gas Company	2- 5-30	Kingston Corp.			62,500.00				
	C. P. Levier & V. D. Behm (5500 Acres approximately)	3-12-30	Duquesne Gas			11,854.00	3,000.00 10.00	8,844.00		11,854.00
	R. C. Tucker Acreage	1-31-30	V. D. Behm	1-31-30	Duquesne Gas	12,000.00		12,000.00		12,000.00
6.	C. V. Garrison, et al	2- 5-30	Kingston Corp.			120,000.00	2,000.00	116,500.00	1,500.00	120,000.00
					Total	$2,572,989.00	$45,510.00	$2,475,379.00	$52,100.00	$2,572,989.00

[fol. 245] PLAINTIFF'S EXHIBIT 12

This consists of an extension agreement executed by C. C. Nuss and J. B. Nuss, Anna Nuss and Ada C. Nuss, and accepted by Kingston Corporation by Otto E. Schuller, Vice President, on the 3rd day of March, 1930, extending the date of the final payment under the contract dated the 5th day of February, 1930, marked Plaintiff's Exhibit No. 2, from March 25, 1930, to April 10, 1930, or prior thereto.

PLAINTIFF'S EXHIBIT 13

This exhibit consists of two documents signed by Victor D. Behm proposing the extension of the date of the final payment from March 25, 1930, to on or prior to April 10, 1930.

These proposals were accepted on the 3rd day of March, 1930, by Kingston Corporation by Otto E. Schuller, Vice President.

PLAINTIFF'S EXHIBIT 14

This exhibit consists of a proposal signed by Raymond Orrill and Charles V. Garrison, proposing to extend the date of the final payment referred to in the contract of February 5, 1930, to April 10, 1930, upon certain terms and conditions.

This proposal was accepted on the 3rd day of March, 1930, by Kingston Corporation, by Otto E. Schuller, Vice-President.

[fol. 246] PLAINTIFF'S EXHIBIT 15

Kingston Corporation,

25 Broad Street, New York, N. Y.

March 12, 1930.

Mr. C. C. Nuss (Ada C. Nuss), Mr. J. B. Nuss (Anna Nuss),
Washington Trust Bldg., Washington, Penna.

DEAR SIRS:

We wish to advise you that the undersigned corporation has made arrangements with Duquesne Gas Corpora-

tion, a corporation organized and existing under the laws of the State of Pennsylvania; by which said corporation will acquire your properties referred to in your Sales Agreement of February 5th, 1930, and we hereby authorize you to deliver to Duquesne Gas Corporation all papers and assignments required.

Very truly yours, Kingston Corporation, by Otto E. Schuller, Vice-President.

CR/CL.

PLAINTIFF'S EXHIBIT 16

This letter, dated March 12, 1930, is addressed by Kingston Corporation by Otto E. Schuller, Vice President, to Mr. C. V. Garrison and Mr. Raymond Orrill, and is similar in form and in content to Plaintiff's Exhibit No. 15.

[fol. 247] PLAINTIFF'S EXHIBIT 17

This consists of a letter dated March 12, 1930, addressed by Kingston Corporation, by Otto E. Schuller, Vice President, to Mr. James S. Gallagher, and is similar in form and in content to Plaintiff's Exhibit No. 15.

PLAINTIFF'S EXHIBIT 18

Kingston Corporation,

52 Wall Street, New York, N. Y.

March 14, 1930.

Mr. C. C. Nuss (Anna Nuss), Mr. J. B. Nuss (Ada Nuss), Washington Trust Building, Washington, Pa.

DEAR SIRS:

In accordance with the agreement between the undersigned Corporation and J. B. Nuss and Anna Nuss and C. C. Nuss and Ada Nuss, dated February 5, 1930, and supplementary agreement, dated March 3, 1930, notice is hereby given you that examination of the property referred

to in Paragraph 1 of the said agreement has been satisfactorily completed and the undersigned elects to proceed in accordance with the said agreement, as supplemented.

Enclosed herewith is our certified check made payable to the order of C. C. Nuss in the amount of Fifteen thousand ($15,000.00) dollars, of which amount, Two thousand [fol. 248] ($2,000.00) dollars is to be paid to C. V. Garrison on or before March 15, 1930.

Please acknowledge receipt of this notice and of the check herewith enclosed.

Very truly yours, Kingston Corporation, by (Signed) Otto E. Schuller, Vice-President.

CR/MHM.
Enc.

PLAINTIFF'S EXHIBIT 19

(Copy)

Washington, Pennsylvania,
March 11, 1930.

To Citizens National Bank, Washington, Pennsylvania.

GENTLEMEN:

There are handed you herewith by the undersigned the following documents:

1. 2 Powers of attorney from H. M. Thompsan et al. to J. B. Nuss and C. C. Nuss, dated February 4th, 1930, and February 1, 1930.

2. Assignment from J. B. Nuss and Anna Nuss and C. C. Nuss and Ada Nuss to Duquesne Gas Corporation, dated March 11, 1930, affecting leasehold estates in Greene and [fol. 249] Washington Counties, Pennsylvania, in duplicate.

3. Assignment from J. B. Nuss, C. C. Nuss, et al., to Duquesne Gas Corporation, dated March 11, 1930, affecting leasehold estates in Greene and Washington Counties, Pennsylvania.

4. Assignment from J. B. Nuss and C. C. Nuss to Duquesne Gas Corporation, dated March 11, 1930, affecting

certain leasehold estates in Greene and Washington Counties, Pennsylvania, in duplicate.

5. Seven assignments of gas sales contracts, each dated March 11, 1930, executed by J. B. Nuss, C. C. Nuss, et al., to Duquesne Gas Corporation, each executed in triplicate.

6. Transfer order on South West Pennsylvania Pipe Lines, dated March 11, 1930, from J. B. Nuss and C. C. Nuss as trustees to Duquesne Gas Corporation, affecting working interest in Elizabeth D. Young oil well, executed in duplicate.

7. Transfer order on South West Pennsylvania Pipe Lines, dated March 11, 1930, from J. B. Nuss and C. C. Nuss as trustees to Duquesne Gas Corporation, affecting working interest in two oil wells on Ella Ray leasehold, executed in duplicate.

to be held and disposed of by you on the following terms and conditions:

1. You are instructed to forward on April 1, 1930, to Equitable Trust Company of New York, a draft in the [fol. 250] amount of six hundred forty-seven thousand dollars ($647,000) drawn on Duquesne Gas Corporation and payable on or before April 10, 1930, with instructions to the said New York bank to notify Furlaud & Company, Inc., 52 Wall Street, New York City, and to permit examination thereof by Furlaud & Company, Inc., and/or by Chapman and Cutler, 57 William Street, New York City, and to advise you at once by telegraph when such draft has been paid.

2. Immediately upon receipt of telegraphic advice from the said New York bank that such draft has been paid, you are instructed to deliver the above enumerated documents handed you herewith to any one of the following named persons, taking his receipt therefor:

(a) Otto E. Schuller, vise president of Duquesne Gas Corporation

(b) Melvin J. Ehrlich, of Chapman and Cutler, Chicago, Illinois

(c) Samuel R. Shambaugh, of Chapman and Cutler, Chicago, Illinois

(d) David Tallant, of Chapman and Cutler, Chicago, Illinois

3. Upon receipt by you of the proceeds of such draft, you are instructed to hold the same subject to the order of the undersigned.

4. It is the intention hereof that in the event the documents above enumerated are delivered by you to the above named persons, or any of them, such delivery shall be deemed to have been made on the date of this letter.

[fol. 251] 5. These instructions may not be revoked or altered except with the written concurrence of Duquesne Gas Corporation, signed by its vice president, or of any one of the above named representatives of Chapman and Cutler, of Chicago.

Yours truly, (Signed) J. B. Nuss, (Signed) C. C. Nuss.

The undersigned acknowledges receipt of the documents above enumerated, and undertakes to hold them subject to the instructions above set forth.

Citizens National Bank, By (Signed) Jno. F. McClay, Cashier.

PLAINTIFF'S EXHIBIT 20

The Equitable Trust Company of New York, 11 Broad Street

Confirmation of message despatched to Citizens National Bank, Washington, Pa.

New York, Apr. 9, 1930.

We hereby confirm the following telegraphic message despatched today.

Your collection 5910 paid we credit your account $647,000.00.

[fol. 252] If this message has not been received by you please notify us immediately.

Very truly yours, J. D. Smith, Authorized Signature.

Capital $500,000.00.
Surplus $1,500,000.00.
John W. Donnan, President, N. R. Baker, Cashier.

Citizens National Bank of Washington

Washington, Pa., April 1, 1930.

Equitable Trust Company
New York, N. Y.

DEAR SIR:

Herewith please find for collection items as stated below. (Protest unless otherwise instructed.)

Jno. F. McClay, Cashier.

No. 5910. From whom received Selves for a/c J. B. Nuss and C. C. Nuss. By whom payable Duquesne Gas Corp. Where payable 52 Wall Street, New York, N. Y. Amount 647,000.00.

Kindly notify Furlaud and Company, Inc., 52 Wall Street, New York City of the arrival of this draft and permit exam- [fol. 253] ination thereof by Furlaud and Company and/or by Chapman and Cutler, 57 William Street, New York City. Advise us by telegraph when the above draft has been paid.

The Equitable Trust Company of New York

City Collection Department,

11 Broad Street, New York

Advice of Credit.

We credit your account proceeds of the collection item described below.

Received 4-2 due 4-10 Dft Yes.

Your number—date 4-1 5910. Description Duquesne Gas Corp. c/o Furlaud & Co. Inc. (wire payt) 52 Wall St. Protest Amount 647,000.00.

Date credited Apr. 9, 1930.

Citizens National Bank

Washington, Pa.

Check or bank draft may have been taken in payment. Credit, therefore, is subject to final payment of such check or draft.

The Equitable Trust Company of New York

Stamp—Paid. We credit your account. The Equitable Trust Company of New York City Collection.

[fol. 254] Foreign Offices London: 10 Moorgate, E. C. 2

Bush House, Aldwych, W. C. 2

Paris: 41 Rue Cambon

Head Office

The Equitable Trust Company of New York

A Merger of

The Seaboard National Bank

The Equitable Trust Company

Member of the Federal Reserve System

11 Broad Street
New York

April 2nd, 1930.

Mr. Jno. F. McClay, Cashier,
Citizens National Bank,
Washington, Pennsylvania.

DEAR SIR:

This will acknowledge receipt of your letter of April 1st, enclosing your collection No. 5910, being a draft drawn on the Duquesne Gas Corporation for $647,000. payable on or before April 10th, 1930.

We communicated with Furlaud & Company and also Messrs. Chapman & Cutler and we understand that this transaction will be taken care of on April 9th.

Just as soon as payment has been received, we shall be glad to advise you by wire.

Very truly yours, (Signed) J. D. Smith, Assistant Secretary.

CH/EW.

[fol. 255] PLAINTIFF'S EXHIBIT 21

$4,000,000

Duquesne Gas Corporation

First Mortgage 6% Convertible Gold Bonds

Dated March 15, 1930. Due March 15, 1945

Distributing Group

Confidential.

New York, March 19, 1930.

Almstead Brothers,
425 West Market Street,
Louisville, Ky.

GENTLEMEN:

We have purchased, when, as and if issued and accepted by us and subject to approval of our counsel $4,000,000 Duquesne Gas Corporation First Mortgage 6% Convertible Gold Bonds, due March 15, 1945, more fully described in the advance circular enclosed herewith.

We are forming a selected group of dealers to distribute this issue and we will act as Distributing Group Managers.

1. Schedule of Prices: The "Offering Price" of these bonds to members of the Distributing Group is 97½% and accrued interest less a net commission of 4% which will be subject to the provisions stated below in case bonds sold to you are repurchased.

You may offer these bonds to the public on March 25, 1930, at the price of 97½% and accrued interest to yield 6.25% to [fol. 256] maturity. From this price, out of your distributing commission of 4% a concession of ¼ of 1% may be allowed by you to banks, dealers, insurance companies, fraternal, educational and charitable organizations and investment trusts. Except as aforesaid, the public offering price must be maintained and no other commission or concessions may be allowed by you to others, whether or not members of this distributing group.

2. Delivery: We expect to make delivery in form of temporary or definitive bonds, or Trustee's interim receipts

therefor on or about April 7, 1930, at the office of Furlaud & Company, Inc., 52 Wall Street, New York, N. Y., against payment in New York funds at 97½% and accrued interest less 1%. The 3% representing the balance of the distributing commission due you will be paid upon termination of the account.

3. Liability: The above sale is made with the understanding that the list price will be maintained until termination of the Distributing Group. We reserve the right to call upon you to take up at our repurchase cost, and you agree to repurchase promptly from us any of the bonds originally delivered to you that are repurchased or contracted for by us at or below 97½% during the life of this Distributing Group, or we may in our discretion retain the concession remaining unpaid to you on Bonds so repurchased.

4. Termination: The life of the Distributing Group will [fol. 257] expire at the close of business on May 26, 1930, unless sooner terminated by us as Managers, but it may be extended in our discretion, for a period or periods not exceeding in the aggregate, sixty days.

5. Reporting Orders: We suggest that you telephone or telegraph your subscription at once to Furlaud & Company, Inc., 52 Wall Street, New York.

6. Circulars and Advertising: A reasonable number of circulars will be furnished on request. You are free to advertise this issue at your own expense after the public advertisement of the undersigned has appeared in New York City.

We reserve the right to make allotments in our discretion and to close the subscription at any time without notice.

Very truly yours, Furlaud & Company, Inc., Bioren & Co., By Furlaud & Company, Inc., Distributing Group Managers.

Furlaud & Company, Inc.,
52 Wall Street, New York, N. Y.

GENTLEMEN:

The undersigned hereby subscribe for $—— principal amount of the above issue of bonds, and agree to be bound

[fol. 258] by all of the terms and provisions as stated hereinabove.

We desire —— circulars with (without) imprint.

.....

Address to which .....
all communications .....
are to be mailed. .....

PLAINTIFF'S EXHIBIT 22

New Issue.

N. Y. Times, March 25, 1930.

$4,000,000

Duquesne Gas Corporation

First Mortgage 6% Convertible Gold Bonds

(Closed Mortgage)

Dated March 15, 1930. Due March 15, 1945.

Principal and semi-annual interest (September 15th and March 15th) payable at the office of the Trustee. Coupon bonds in denominations of $1,000 and $500. Registerable as to principal. Redeemable as a whole or in part on any interest date, upon thirty days' published notice, to and including March 15, 1935, at 105 and accrued interest, the redemption premium decreasing one-half of one per cent during each year thereafter. Interest payable without deduction for that portion of any Federal income tax not in excess of two per cent. Refund of certain California, Con-
[fol. 259] necticut, District of Columbia, Iowa, Kansas, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, Oregon and Virginia taxes upon timely and proper application, as provided in the mortgage. Tax free in Pennsylvania. Central Hanover Bank and Trust Company, New York, Trustee.

These bonds are convertible on or after November 15, 1930, into shares of the Common Stock of Duquesne Gas Corporation, as constituted at the time of conversion, on

the following basis: 80 shares for each $1,000 bond surrendered for conversion on or after November 15, 1930, and up to and including March 15, 1935; 65 shares for each $1,000 bond surrendered for conversion after March 15, 1935, and up to and including March 15, 1940; 50 shares for each $1,000 bond surrendered for conversion after March 15, 1940, and prior to maturity.

The following is quoted from a letter from the Vice-President of the Corporation to the bankers:

Business: Duquesne Gas Corporation, incorporated under the laws of the State of Pennsylvania, and its subsidiary will own and operate properties which are now producing, transporting, and distributing natural gas in Western Pennsylvania. Over 99% of all gas produced is sold under contract to large industrial enterprises and to leading public utility companies supplying the domestic and industrial requirements of Pittsburgh and vicinity. The properties are located within a radius of from seven to forty-five miles of Pittsburgh. This exceptionally favorable location in one of the country's most highly developed [fol. 260] industrial sections assures a permanent and growing market for the Corporation's output.

The customers of Duquesne Gas Corporation and its subsidiary include The Peoples Natural Gas Company and Columbia Natural Gas Company, subsidiaries of Standard Oil Company of New Jersey; Equitable Gas Company, subsidiary of Philadelphia Company; Manufacturers Light & Heat Company and Greensboro Gas Company, subsidiaries of Columbia Gas & Electric Corporation; State Line Gas Company, subsidiary of West Penn Electric Company; and Westinghouse Electric & Manufacturing Company and its subsidiaries.

The Corporation will own 147 gas wells and will control through lease, or own in fee, gas rights in over 40,000 acres of land in the gas-producing territories of nine adjacent counties encircling the City of Pittsburgh.

Security: These bonds will be secured, in the opinion of counsel, by a first closed mortgage on all of the fixed physical properties and developed leases of the Corporation, now owned and hereafter acquired, subject to outstanding contracts for the sale of gas and the usual farm mortgages. The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, ag-

gregate $7,038,000, the properties examined by Mattison, Davey & Winters, New York, being appraised at $4,929,787 and those examined by Ralph E. Davis, Pittsburgh, Pa., at $1,743,520.

Earnings: Consolidated earnings for the properties, have been certified by Barrow, Wade, Guthrie & Co. for the calendar year 1929. For the calendar years 1930, 1931 and [fol. 261] 1932, based upon the successful consummation of the drilling program and the sale of the gas so developed under existing contracts earnings have been computed by the engineers as follows: *

	1929	1930	1931	1932
Gross Revenue	$614,406	$953,353	$1,113,716	$1,203,749
Operating expenses, maintenance and taxes (not Including Federal Income Tax)	80,800	120,321	133,807	148,075
Net earnings available for interest, depreciation, depletion and Federal Income Tax	$533,606	$833,032	$979,909	$1,055,674
Maximum annual interest requirements of this issue		$240,000		

The average of estimated earnings for the three years 1930, 1931 and 1932 indicate net earnings of approximately 4 times such maximum annual interest requirements.

Capitalization: Upon completion of this financing, the Corporation's capitalization will be as follows:

	Authorized	Outstanding
First Mortgage 6% Convertible Gold Bonds (this issue)	$4,000,000	$4,000,000

[fol. 262]

Five Year Convertible 6½% Secured Gold Notes†	1,000,000	1,000,000
Common Stock (no par value)	‡1,250,000 Shares	675,000 Shares

† Secured by pledge with the Trustee of an equal principal amount of General Mortgage 6½% Gold Bonds, due March 15, 1940.

‡ Including 400,000 shares reserved for conversion of the Bonds and Notes.

Sinking Fund: The mortgage will provide for a fixed sinking fund payable monthly to the Trustee, beginning June 10, 1931, and for an additional annual sinking fund

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* Mattison, Davey & Winters and Ralph E. Davis estimate net earnings of the properties examined by them, respectively, as follows: 1930, $543,145 and $289,887; 1931, $666,388 and $313,521; 1932, $743,124 and $312,550. The totals of these amounts represent the estimated net earnings as stated above.

payable out of earnings, as provided in the mortgage, calculated to retire this entire issue prior to maturity.

Gas reserves, valuations, estimated earnings and other engineering features have been reported upon by Mattison, Davey & Winters, New York, for the properties in Fayette, Greene and Washington Counties, Pennsylvania, and Monongalia and Preston Counties, West Virginia, and by Ralph E. Davis, Pittsburgh, Pa., for the properties in Allegheny, Armstrong, Westmoreland and Indiana Counties, Pennsylvania. Accounts have been examined by Barrow, Wade, Guthrie & Co., New York, as of December 31, 1929. Legal matters are under supervision of Chapman & Cutler. These bonds are offered for delivery when, as and if issued and accepted by us, subject to the approval of counsel. Original delivery may be made in the form of Trustee's interim receipts or temporary bonds, exchangeable for definitive bonds.

The Corporation has agreed to make application to list these bonds on the New York Curb Exchange.

[fol. 263] Price 97½ and Accrued Interest to Yield 6.25 Per Cent

Furlaud & Company, Inc.

Bioren & Co., Hincks Bros. & Co., Bradford, Kimball & Co., C. H. Huston & Co., Inc.

The information contained herein, while not guaranteed, has been obtained from sources believed to be reliable.

PLAINTIFF'S EXHIBIT 23

New Issue.

$4,000,000

Duquesne Gas Corporation

First Mortgage 6% Convertible Gold Bonds

(Closed Mortgage)

Dated March 15, 1930. Due March 15, 1945.

Principal and semi-annual interest (September 15th and March 15th) payable at the office of the Trustee. Coupon bonds in denominations of $1,000 and $500. Registerable as to principal. Redeemable as a whole or in part on any interest date, upon thirty days' published notice, to and

including March 15, 1935, at 105 and accrued interest, the redemption premium decreasing one-half of one per cent during each year thereafter. Interest payable without deduction for that portion of any Federal income tax not in excess of two per cent. Refund of certain California, Connecticut, District of Columbia, Iowa, Kansas, Kentucky, [fol. 264] Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, Oregon and Virginia taxes upon timely and proper application, as provided in the mortgage.

Tax Free in Pennsylvania

Central Hanover Bank and Trust Company, New York, Trustee

The mortgage will provide for a fixed sinking fund payable monthly to the Trustee beginning June 10, 1931, and for an additional sinking fund payable out of earnings, as provided in the mortgage, calculated to retire this entire issue prior to maturity.

The properties of Duquesne Gas Corporation supply gas at wholesale to prominent public utility and industrial companies in Pennsylvania. The subsidiary operates under the jurisdiction of The Public Service Commission of the State of Pennsylvania.

The following is quoted from a letter from the Vice-President of the Corporation to the bankers:

Business

Duquesne Gas Corporation has been incorporated under the laws of the State of Pennsylvania to acquire, own and [fol. 265] operate natural gas properties in Pennsylvania and West Virginia now supplying gas under contract to The Peoples Natural Gas Company and Columbia Natural Gas Company, subsidiaries of Standard Oil Company of New Jersey; to Equitable Gas Company, subsidiary of Philadelphia Company; to Manufacturers Light & Heat Company and Greensboro Gas Company, subsidiaries of Columbia Gas & Electric Corporation; to State Line Gas Company, subsidiary of West Penn Electric Company; and to Bellewood & Monongahela City Natural Gas Company, Westinghouse Electric & Manufacturing Company, Westinghouse Machine Company, Westinghouse Foundry Company, and Wynn Brick Company.

The properties of the Corporation and its subsidiary are located in the gas producing territories of Armstrong,

Allegheny, Westmoreland, Washington, Greene and Fayette Counties which surround the City of Pittsburgh. The Corporation controls additional gas reserves in Indiana County, Pennsylvania, and in Monongalia and Preston Counties, West Virginia. The Corporation's subsidiary, Victor Gas Company, owns a strategically located pipe line in Fayette County, Pennsylvania.

The Corporation owns 155 gas wells and controls through lease, or owns in fee, the gas rights in over 40,000 acres of land. The properties of the Corporation produced more than 2,600,000,000 cubic feet of gas during the year 1929.

Security

These bonds are secured, in the opinion of counsel, by a first closed mortgage on all of the fixed physical properties [fol. 266] and developed leases of the Corporation, now owned and hereafter acquired, subject to outstanding contracts for the sale of gas and the usual farm mortgages.

The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, aggregate $7,038,000, the properties examined by Mattison, Davey & Winters, New York, being appraised at $4,929,787 and those examined by Ralph E. Davis, Pittsburgh, Pa., at $1,743,520.

Earnings

Consolidated earnings of the properties, as certified by Barrow, Wade, Guthrie & Co. for the calendar year 1929, and as estimated by the engineers for the years 1930, 1931 and 1932, are shown below:*

	1929	1930	1931	1932
Gross Revenue	$614,406	$953,353	$1,113,716	$1,203,049
Operating expenses, maintenance and taxes (not including Federal Income Tax)	80,800	120,321	133,807	148,075
Net earnings available for interest, depreciation, depletion and Federal Income Tax	$533,606	$833,032	$979,909	$1,055,674
Maximum annual interest requirements of this issue		$240,000		

*Mattison, Davey & Winters and Ralph E. Davis estimate net earnings of the properties examined by them, respectively, as follows: 1930, $543,145 and $289,887; 1931, $666,388 and $313,521; 1932, $743,124 and $312,550. The totals of these amounts represent the estimated net earnings as stated above.

[fol. 267] The average of estimated earnings for the three years 1930, 1931 and 1932 indicate net earnings of approximately 4 times such maximum annual interest requirements.

Capitalization

	Authorized	Outstanding
First Mortgage 6% Convertible Gold Bonds (this issue)	$4,000,000	$4,000,000
Convertible 6½% Secured Gold Notes*	1,000,000	1,000,000
Common Stock (no par value)	** 1,250,000 Shares	675,000 Shares

* Secured by pledge with the Trustee of an equal principal amount of General Mortgage 6½% Gold Bonds, due March 15, 1940.

** Including 400,000 shares reserved for conversion of the Bonds and Notes.

Gas Reserves

The gas reserves of the acreage controlled by Duquesne Gas Corporation have been reported by the engineers to be over 82,000,000,000 cubic feet, being the aggregate of 63,000,000,000 cubic feet, reported by Mattison, Davey & Winters and 19,000,000,000 cubic feet reported by Ralph E. Davis. The earnings to be derived from these reserves, as estimated by the engineers, are more than sufficient for the complete amortization of the bonds and notes of Duquesne Gas Corporation.

Markets

The properties of Duquesne Gas Corporation are all located within a radius of from seven to forty-five miles of [fol. 268] Pittsburgh. This densely populated and highly industrialized section of the country assures a permanent and rapidly growing market for the Corporation's output. All the gas produced by the Corporation is sold direct to large industrial enterprises and to prominent public utility companies supplying the domestic and industrial requirements of Pittsburgh and vicinity.

Over 99% of all gas produced is sold under contract. Principal customers and locations of supplying properties are listed below:

Name of Purchaser and Location of Supplying Properties:

The Peoples Natural Gas Company, Armstrong, Washington and Westmoreland Counties; Columbia Natural Gas

Company, Washington County (subsidiaries of Standard Oil Company of New Jersey).

Equitable Gas Company, Allegheny, Washington and Westmoreland Counties (subsidiary of Philadelphia Company).

Manufacturers Light & Heat Company, Greene and Washington Counties; Greensboro Gas Company, Washington County (subsidiaries of Columbia Gas & Electric Corporation).

State Line Gas Company, Fayette County (subsidiary of West Penn Electric Company).

[fol. 269] Westinghouse Electric & Manufacturing Company, Allegheny County.

Westinghouse Machine Company, Allegheny County.

Westinghouse Foundry Company, Allegheny County.

Pittsburgh Plate Glass Company, Armstrong and Westmoreland Counties.

Other large customers of the Corporation include Wynn Brick Company and Bellewood & Monogahela City Natural Gas Company.

The Corporation has under consideration an expansion program involving the acquisition of certain new properties which should materially increase the Corporation's gas production and sales.

Conversion

These bonds are convertible on or after November 15, 1930, into shares of the Common Stock of Duquesne Gas Corporation, as constituted at the time of conversion, on the following basis:

80 shares for each $1,000 bond surrendered for conversion on or after November 15, 1930, and up to and including March 15, 1935;

65 shares for each $1,000 bond surrendered for conversion after March 15, 1935, and up to and including March 15, 1940;

50 shares for each $1,000 bond surrendered for conversion after March 15, 1940, and prior to maturity.

Each $500 bond is convertible into a proportionate number of shares of Common Stock. In case of redemption the con- [fol. 270] version privilege pertaining to each bond may be exercised up to and including the redemption date.

Sinking Fund

The mortgage will provide for a fixed sinking fund payable monthly to the Trustee, beginning June 10, 1931, and for an additional annual sinking fund payable out of earnings, as provided in the mortgage, calculated to retire this entire issue prior to maturity. The Corporation may deposit either cash or bonds at par, and the Trustee will use the cash thus deposited for the purchase of bonds at not exceeding the then call price. In the event that bonds cannot be purchased at or at less than the call price, the Trustee will call bonds by lot through publication.

Purpose of Issue

These bonds are issued by the Corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes.

Management

The properties of the Corporation will continue under the management of the men who have been largely responsible for their successful operation in the past. Consultant Managers will be Mattison, Davey & Winters, New York.

Gas reserves, valuations, estimated earnings and other engineering features have been reported upon by Mattison, [fol. 271] Davey & Winters, New York, for the properties in Fayette, Greene and Washington Counties, Pennsylvania, and Monongalia and Preston Counties, West Virginia, and by Ralph E. Davis, Pittsburgh, Pa., for the properties in Allegheny, Armstrong, Westmoreland and Indiana Counties, Pennsylvania. Accounts have been examined by Barrow, Wade, Guthrie & Co., New York, as of December 31, 1929. Legal matters are under the supervision of Chapman & Cutler.

Listed on the New York Curb Exchange

Price at Market

The information contained herein, while not guaranteed, has be-n obtained from sources believed to be reliable.

PLAINTIFF'S EXHIBIT 24

N. Y. Times—April 29, 1930.

New Issue.

$1,000,000

Duquesne Gas Corporation

Convertible 6½% Secured Gold Notes

Dated March 15, 1930. Due March 15, 1935

Principal and semi-annual interest (September 15th and March 15th) payable at the office of the Trustee. Coupon notes in denominations of $1,000 and $500. Registerable as to principal. Redeemable as a whole or in part on any inter- [fol. 272] est date, upon thirty days' published notice, to and including September 15, 1931, at 105 and accrued interest, the redemption premium decreasing one per cent during each year thereafter. Interest payable without deduction for that portion of any Federal income tax not in excess of two per cent. Refund of certain California, Connecticut, District of Columbia, Iowa, Kansas, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, Oregon and Virginia taxes upon timely and proper application, as provided in the trust agreement. Pacific Trust Company, New York, Trustee.

Tax Free in Pennsylvania

Each $1,000 Note is convertible on or after November 15, 1930 and prior to maturity into 80 shares of the Common Stock of Duquesne Gas Corporation, as constituted at the time of conversion. Each $500 Note is convertible into a proportionate number of shares of Common Stock. In case of redemption the conversion privilege pertaining to each Note may be exercised up to and including the redemption date.

The following is quoted from a letter from the Vice-President of the Corporation to the bankers:

Business: Duquesne Gas Corporation, incorporated under the laws of the State of Pennsylvania, and its subsidiary own and operate properties which are producing, transport-

ing and distributing natural gas in Western Pennsylvania. Over 99% of all gas produced is sold under contract to large industrial enterprises and to leading public utility companies supplying the domestic and industrial requirements of [fol. 273] Pittsburgh and vicinity. The properties are located within a radius of from seven to forty-five miles of Pittsburgh. This exceptionally favorable location in one of the country's most highly developed industrial sections assures a permanent and growing market for the Corporation's output.

The customers of Duquesne Gas Corporation and its subsidiary include The Peoples Natural Gas Company and Columbia Natural Gas Company, subsidiaries of Standard Oil Company of New Jersey; Equitable Gas Company, subsidiary of Philadelphia Company; Manufacturers Light & Heat Company and Greensboro Gas Company, subsidiaries of Columbia Gas & Electric Corporation; State Line Gas Company, subsidiary of West Penn Electric Company; and Westinghouse Electric & Manufacturing Company and its subsidiaries.

The Corporation owns 152 gas wells and controls through lease, or owns in fee, gas rights in over 40,000 acres of land in the gas-producing territories of nine adjacent counties encircling the City of Pittsburgh.

Security: These notes, in the opinion of counsel, will be a direct obligation of Duquesne Gas Corporation and will be secured by pledge with the Trustee of an equal principal amount of General Mortgage 6½% Gold Bonds, due March 15, 1940. The General Mortgage 6½% Gold Bonds, in the opinion of counsel, will be secured by a general mortgage on all of the fixed physical properties and developed leases of the Corporation, now owned and hereafter acquired, subject to $4,000,000 First Mortgage 6% Convertible Gold Bonds, due March 15, 1945, and to outstanding contracts for the sale of gas and the usual farm mortgages. The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, aggregate $7,038,000 [the properties examined by Mattison, Davey & Winters, New York, being appraised at $4,929,787 and those examined by Ralph E. Davis, Pittsburgh, Pa., at $1,743,520], which value after deducting the principal amount of First Mortgage Bonds, represents more than $3,000 for each $1,000 principal amount of these Notes. [fol. 274]

Earnings: Consolidated earnings of the properties, as certified by Barrow, Wade, Guthrie & Co. for the calendar year 1929, and as estimated by the engineers for the years 1930, 1931 and 1932, are shown below:*

	1929	1930	1931	1932
Gross Revenue	$614,406	$953,353	$1,113,716	$1,203,749
Operating expenses, maintenance and taxes (not including Federal Income Tax)	80,800	120,321	133,807	148,075
Net earnings available for interest, depreciation, depletion and Federal Income Tax	$533,606	$833,032	$979,909	$1,055,674
Interest and fixed sinking fund requirements of the First Mortgage Bonds	240,000	240,000	289,000	324,000
Balance	$293,606	$593,032	$ 690,909	$731,674
Maximum annual interest requirements of this issue		$65,000		

[fol. 275] Available earnings for 1929, as shown above, were equal to over 4½ times maximum annual interest requirements of this issue, and the average balance for the three years 1930, 1931 and 1932 is estimated to exceed 10 times such interest requirements.

Sinking Fund: The trust agreement under which these notes are issued will provide for a fixed sinking fund payable monthly to the Trustee, beginning June 10, 1930, and for an additional annual sinking fund payable out of earnings as provided in the trust agreement, calculated to retire approximately 50% of this issue prior to maturity.

Gas reserves, valuations, estimated earnings and other engineering features have been reported upon by Mattison, Davey & Winters, New York, for the properties in Fayette, Greene and Washington Counties, Pennsylvania, and Monongalia and Preston Counties, West Virginia, and by Ralph E. Davis, Pittsburgh, Pa., for the properties in Allegheny, Armstrong, Westmoreland and Indiana Counties, Pennsylvania. Accounts have been examined by

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* Mattison, Davey & Winters and Ralph E. Davis estimate net earnings of the properties examined by them respectively, as follows: 1930, $543,145 and $289,887; 1931, $666,388 and $313,521; 1932, $743,124 and $312,550. The totals of these amounts represent the estimated net earnings as stated above.

Barrow, Wade, Guthrie & Co., New York, as of December 31, 1929. Legal matters are under supervision of Chapman & Cutler. These are offered for delivery when, as and if issued and accepted by us, subject to the approval of counsel. Original delivery may be made in the form of Trustee's interim receipts or temporary notes, exchangeable for definitive notes.

Price 98 and Accrued Interest to Yield About 7%

Furlaud & Company, Inc. Cullen & Drew.

[fol. 276] The information contained herein, while not guaranteed, has been obtained from sources believed to be reliable.

PLAINTIFF'S EXHIBIT 25

New Issue Proof—Subject to Change

$1,000,000

Duquesne Gas Corporation

Convertible 6½% Secured Gold Notes

Dated March 15, 1930. Due March 15, 1935

Principal and semi-annual interest (September 15th and March 15th) payable at the office of the Trustee. Coupon notes in denominations of $1,000 and $500. Registerable as to principal. Redeemable as a whole or in part on any interest date, upon thirty days, published notice, to and including September 15, 1931, at 105 and accrued interest, the redemption premium decreasing one per cent during each year thereafter. Interest payable without deduction for that portion of any Federal income tax not in excess of two per cent. Refund of certain California, Connecticut, District of Columbia, Iowa, Kansas, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, New Hampshire, Oregon and Virginia taxes upon timely and proper application, as provided in the trust agreement.

[fol. 277] Tax Free in Pennsylvania

Pacific Trust Company, New York, Trustee

The properties of Duquesne Gas Corporation supply gas at wholesale to prominent public utility and industrial companies in Pennsylvania. The subsidiary operates under the jurisdiction of The Public Service Commission of the State of Pennsylvania.

The following is quoted from a letter from the Vice-President of the Corporation to the bankers:

Business

Duquesne Gas Corporation has been incorporated under the laws of the State of Pennsylvania to acquire, own and operate natural gas properties in Pennsylvania and West Virginia now supplying gas under contract to The Peoples Natural Gas Company and Columbia Natural Gas Company, subsidiaries of Standard Oil Company of New Jersey; to Equitable Gas Company, subsidiary of Philadelphia Company; to Manufacturers Light & Heat Company and Greensboro Gas Company, subsidiaries of Columbia Gas & Electric Corporation; to State Line Gas Company, subsidiary of West Penn Electric Company; and to Bellewood & Monongahela City Natural Gas Company, Westinghouse Electric & Manufacturing Company, Westinghouse Machine Company, Westinghouse Foundry Company, and Wynn Brick Company.

[fol. 278] The properties of the Corporation and its subsidiary are located in the gas producing territories of Armstrong, Allegheny, Westmoreland, Washington, Greene and Fayette Counties which surround the City of Pittsburgh. The Corporation controls additional gas reserves in Indiana County, Pennsylvania, and in Monongalia and Preston Counties, West Virginia. The Corporation's subsidiary, Victor Gas Company, owns a strategically located pipe line in Fayette County, Pennsylvania.

The Corporation will own 147 gas wells and will control through lease, or own in fee, the gas rights in over 40,000 acres of land. The properties of the Corporation produced more than 2,600,000,000 cubic feet of gas during the year 1929.

Security

These notes, in the opinion of counsel, will be a direct obligation of Duquesne Gas Corporation and will be se-

cured by pledge with the Trustee of an equal principal amount of General Mortgage 6½% Gold Bonds, due March 15, 1940. The General Mortgage 6½% Gold Bonds, in the opinion of counsel, will be secured by a general mortgage on all of the fixed physical properties and developed leases of the Corporation, now owned and hereafter aqcuired, subject to $4,000,000 First Mortgage 6% Convertible Gold Bonds, due March 15, 1945, and to outstanding contracts for the sale of gas and the usual farm mortgages.

The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, aggregate $7,038,000 [the properties examined by Mattison, Davey & Winters, New York, being appraised at [fol. 279] $4,929,787 and those examined by Ralph E. Davis, Pittsburgh, Pa., at $1,743,520], which value, after deducting the principal amount of First Mortgage Bonds, represents more than $3,000 for each $1,000 principal amount of these Notes.

Earnings

Consolidated earnings of the properties, as certified by Barrow, Wade, Guthrie & Co. for the calendar year 1929, and as estimated by the engineers for the years 1930, 1931 and 1932, are shown below:*

	1929	1930	1931	1932
Gross Revenue	$614,406	$953,353	$1,113,716	$1,203,749
Operating expenses, maintenance and taxes (not including Federal Income Tax)	80,800	120,321	133,807	148,075
Net earnings available for interest, depreciation, depletion and Federal Income Tax	$533,606	$833,032	$979,909	$1,055,674
Interest and fixed sinking fund requirements of the First Mortgage Bonds	240,000	240,000	289,000	324,000
Balance	$293,606	$593,032	$ 690,909	$731,674
Maximum annual interest requirements of this issue		$65,000		

*Mattison, Davey & Winters and Ralph E. Davis estimate net earnings of the properties examined by them respectively, as follows: 1930, $543,145 and $289,887; 1931, $666,388 and $313,521; 1932, $743,124 and $312,550. The totals of these amounts represent the estimated net earnings as stated above.

[fol. 280] Available earnings for 1929, as shown above, were equal to over 4½ times maximum annual interest requirements of this issue, and the average balance available for the three years 1930, 1931 and 1932 is estimated to exceed 10 times such interest requirements.

Capitalization

Upon completion of this financing, the Corporation's capitalization will be as follows:

	Authorized	Outstanding
First Mortgage 6% Convertible Gold Bonds	$4,000,000	$4,000,000
Convertible 6½% Secured Gold Notes (this issue)†	1,000,000	1,000,000
Common Stock (no par value)	‡1,250,000 Shares	675,000 Shares

† Secured by pledge with the Trustee of an equal principal amount of General Mortgage 6½% Gold Bonds, due March 15, 1940.

‡ Including 400,000 shares reserved for conversion of the Bonds and Notes.

Gas Reserves

The gas reserves of the acreage controlled by Duquesne Gas Corporation have been reported by the engineers to be over 82,000,000,000 cubic feet, being the aggregate of 63,000,000,000 cubic feet reported by Mattison, Davey & Winters and 19,000,000,000 cubic feet reported by Ralph E. Davis. The earnings to be derived from these reserves, as estimated by the engineers, are more than sufficient for the complete amortization of the bonds and notes of Duquesne Gas Corporation.

[fol. 281]

Markets

The properties of Duquesne Gas Corporation are all located within a radius of from seven to forty-five miles of Pittsburgh. This densly populated and highly industrialized section of the country assures a permanent and rapidly growing market for the Corporation's output. All the gas produced by the Corporation is sold direct to large industrial enterprises and to prominent public utility companies supplying the domestic and industrial requirements of Pittsburgh and vicinity.

Over 99% of all gas produced is sold under contract. Principal customers and locations of supplying properties are listed below:

Name of purchaser and location of supplying properties:

The Peoples Natural Gas Company, Armstrong, Washington and Westmoreland Counties.
Columbia Natural Gas Company, Washington County. (Subsidiaries of Standard Oil Company of New Jersey.)
Equitable Gas Company, Allegheny, Washington and Westmoreland Counties. (Subsidiary of Philadelphia Company)
Manufacturers Light & Heat Company, Greene and Washington Counties.
Greensboro Gas Company, Washington County. (Subsidiaries of Columbia Gas & Electric Corporation.)
[fol. 282] State Line Gas Company, Fayette County. (Subsidiary of West Penn. Electric Company.)
Westinghouse Electric & Manufacturing Company, Allegheny County.
Westinghouse Machine Company, Allegheny County.
Westinghouse Foundry Company, Allegheny County.
Pittsburgh Plate Glass Company, Armstrong and Westmoreland Counties.

Other large customers of the Corporation include Wynn Brick Company and Bellewood & Monongahela City Natural Gas Company.

The Corporation has under consideration an expansion program involving the acquisition of certain new properties which should materially increase the Corporation's gas production and sales.

Conversion

Each $1,000 note is convertible on or after November 15, 1930, and prior to maturity into 80 shares of the Common Stock of Duquesne Gas Corporation, as constituted at the time of conversion. Each $500 Note is convertible into a proportionate number of shares of Common Stock. In case of redemption the conversion privilege pertaining to each Note may be exercised up to and including the redemption date.

[fol. 283]

Sinking Fund

The trust agreement under which these notes are issued will provide for a fixed sinking fund payable monthly to the

Trustee, begining June 10, 1930, and for an additional annual sinking fund payable out of earnings, as provided in the trust agreement, calculated to retire approximately 50% of this issue prior to maturity. The Corporation may deposit either cash or notes at par, and the Trustee will use the cash thus deposited for the purchase of notes at not exceeding the then call price. In the event that notes cannot be purchased at or at less than the call price, the Trustee will call notes by lot through publication. Upon the retirement of any notes, a like principal amount of General Mortgage Bonds will be cancelled.

Purpose of Issue

These Notes are issued by the Corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes.

Management

The properties of the Corporation will continue under the management of the men who have been largely responsible for their successful operation in the past. Consultant Managers will be Mattison, Davey & Winters, New York.

Gas reserves, valuations, estimated earnings and other [fol. 284] engineering features have been reported upon by Mattison, Davey & Winters, New York, for the properties in Fayette, Greene and Washington Counties, Pennsylvania, and Monongalia and Preston Counties, West Virginia, and by Ralph E. Davis, Pittsburgh, Pa., for the properties in Allegheny, Armstrong, Westmoreland and Indiana Counties, Pennsylvania. Accounts have been examined by Barrow, Wade, Guthrie & Co., New York, as of December 31, 1929. Legal matters are under the supervision of Chapman & Cutler.

These notes are offered for delivery when, as and if issued and accepted by us, subject to the approval of counsel.

Original delivery may be made in the form of Trustee's interim receipts or temporary notes, exchangeable for definitive notes.

Price 98 and Accrued Interest to Yield about 7 Per Cent

The information contained herein, while not guaranteed, has been obtained from sources believed to be reliable.

[fol. 285] PLAINTIFF'S EXHIBIT 26

Duquesne Gas Corporation

First Mortgage 6% Convertible Gold Bonds

Due March 15, 1945

Secondary Distributing Group

Confidential.

New York, August 14, 1930.

DEAR SIRS:

We are forming a Secondary Distributing Group of which we will be the Managers and in which we are pleased to include you, to distribute the First Mortgage 6% Convertible Gold Bonds of Duquesne Gas Corporation. You will have no commitment in this Group except to take up and pay for the number of bonds ordered by you and delivered to you by us. Payment of bonds allotted to you is to be made upon delivery of bonds to you.

This offering is to be made only on and after the above date to bona fide investors by the Distributing Group at the closing price of the said bonds on the New York Curb as of the night before order is received by us unless you are advised by telegraph of any change in price.

Orders will be received for any number of bonds from any member of the Distributing Group, but we reserve the right from time to time to limit the number of bonds to be sold to any one member.

Upon such bonds ordered from us and allotted and delivered to you which are paid for by you and which are not repurchased by us or which we do not contract to repur-[fol. 286] chase during a period of sixty (60) days from date of delivery of such bonds to you, we will pay you:

A commission of 2 points on sales up to 15 bonds;

A commission of 3 points on sales over 15 and up to 25 bonds;

A commission of 3½ points on sales over 25 and up to 50 bonds;

A commission of 4 points on sales over 50 bonds.

We will advance to you one-half of the commission, as per above schedule, by allowing you to deduct one-half of

the commission on each lot of bonds delivered to you when you remit for bonds allotted to you. Settlements on balances of commissions due will be made by us sixty days (60) after each delivery of bonds which are not repurchased, or which we do not contract to repurchase within sixty (60) days from date of delivery to you. Bonds will not be considered sold in calculating commissions due you if they are so repurchased or contracted for.

You agree to return the commissions deducted by or paid to you as aforesaid on any bonds so repurchased or contracted for within 60 days from delivery to you.

Orders should be telegraphed directly to us for confirmation and no order shall be binding on us unless confirmed by us. We reserve the right in our uncontrolled discretion to confirm orders in whole or in part, or to reject orders in whole or in part.

This agreement may be terminated at one day's written or telegraphic notice but such termination shall not affect [fol. 287] the right of the members to commissions on sales of bonds made prior thereto which we do not repurchase or contract to repurchase within sixty days from date of delivery.

If you desire to participate in this distributing group, kindly indicate your acceptance by signing the duplicate attached hereto and returning it to us.

Yours very truly, Furlaud, Reuter & Co., Incorporated, by —— ——, Managers.

Attached thereto is a duplicate with the following at the bottom of the sheet in the lower left hand corner thereof: "Accepted: By —— ——, Date —— —, ——."

PLAINTIFF'S EXHIBIT 27

This exhibit consists of the minute books of Duquesne Gas Corporation, being five volumes in number. Contained in Plaintiff's Exhibit No. 27 are Defendant's Exhibits E, F and G to which reference is hereby made.

[fol. 288] PLAINTIFF'S EXHIBIT 28

No. 1. New York, April 9th, 1930.

Central Hanover Bank and Trust Company

Seventy Broadway 1-33

(perforated)
C H B & T
4 10 30

Pay to the order of Central Hanover Bank and Trust Company $3,015,000.00 Three million fifteen thousand 00/100 Dollars

Robert Halporn, Ass't Treas.

Carlos Reuter, Pres.

[Duquesne Gas Corporation.]

PLAINTIFF'S EXHIBITS 29 AND 30

These exhibits are books of account of Furlaud, Reuter & Co., Inc.

The contents of these books are voluminous and the parts of those books which were referred to in the testimony have been incorporated in the proposed narrative form.

[fol. 289] PLAINTIFF'S EXHIBIT 31

This exhibit is a letter addressed by Chaucer Corporation and Byron Corporation under date of May 29, 1930, to John J. Bergen, 120 Broadway, New York City, and confirmed by him on that date. Said agreement was signed by Chaucer Corporation, by Carlos Reuter, President, and by Byron Corporation, by James P. Cleaver, President.

It grants an option to John J. Bergen to purchase all or any part of 100,000 shares of the Common Stock of Duquesne Gas Corporation at the price of $10.00 per share, a further option to purchase all or any part of 150,000 shares (in addition to the previous 100,000 shares) at $12.50 per share and a further option to purchase 50,000 shares at $14.00 per share.

These options were granted upon certain terms and conditions.

Annexed to said agreement is the following guarantee by Furlaud & Company:

"Furlaud & Company, Inc., being greatly interested in the performance of the foregoing agreement, and being desirous that John J. Bergen shall enter into the foregoing contract does, in order to induce him to enter into and execute the same, hereby guarantee performance of the obligations of the Chaucer Corporation and the Byron Corporation under the terms and provisions of the foregoing contract.

Dated, New York, May 29, 1930.

Furlaud & Company, By M. H. Furlaud (Seal) President."

[fol. 290] DEFENDANT'S EXHIBIT A

Agreement of reorganization between Kingston Corporation, a corporation organized and existing under the laws of the State of New Jersey (hereinafter sometimes called "Kingston") and Duquesne Gas Corporation, a corporation organized and existing under the laws of the Commonwealth of Pennsylvania, (hereinafter sometimes called "Duquesne"),

Witnesseth:

Whereas, Kingston has entered into various agreements entitling and obligating it to purchase the properties hereinafter referred to and has arranged to obtain funds necessary to effect its acquisition of such properties, and

Whereas, Duquesne desires to acquire the said properties, and

Whereas, both Kingston and Duquesne have determined that it is to their best interest that the following plan of reorganization be adopted.

Now, therefore, this agreement further witnesseth, That for and in consideration of the premises and of the agreements herein contained, the parties hereto do hereby agree upon and adopt the following plan of reorganization.

1. Kingston will acquire the properties described in Schedule A hereto annexed and made a part hereof, which proper-

ties will constitute all of Kingston's assets other than cash, and will cause said properties to be transferred, assigned and conveyed unto Duquesne, thus transferring to Duquesne substantially all of its assets. Kingston will pay all charges [fol. 291] for fees and expenses of auditors, counsel, engineers and brokers incurred incident to such acquisition.

2. Kingston represents that it is or will be obligated to Central Hanover Bank & Trust Company for the sum of $3,015,000 and in order to effect this reorganization and transfer of assets Duquesne will and does hereby assume and promise to pay promptly such obligation in the amount of $3,015,000 upon its being assured to its satisfaction that the aforesaid properties have been so transferred, assigned and conveyed to it. Also upon such assurance to Duquesne with respect to said properties and in exchange therefor, Duquesne will promptly issue to Kingston 535,000 shares of its Common Stock, without nominal or par value, together with $1,300,000 principal amount of its First Mortgage 6% Convertible Gold Bonds, dated March 15, 1930, and issued under and secured by an indenture between Duquesne and Central Hanover Bank & Trust Company, dated March 15, 1930. Kingston agrees for itself and any subsequent holders of the aforesaid shares of Common Stock of the Corporation that upon any issue for money or other consideration of other shares of stock or any bonds convertible into stock of the Corporation, whether now or hereafter authorized, neither it nor they nor any of them shall be entitled of right by reason of holding stock of the Corporation to subscribe for, purchase or receive any of such stock or bonds so issued but the Board of Directors may dispose of all or any of such stock or bonds without offering the same in the first instance to the stockholders for subscription or purchase.

[fol. 292] 3. Delivery of said shares and bonds by Duquesne shall be conclusive evidence of the acceptance by Duquesne of the aforesaid properties and shall release Kingston from any and all further responsibility with respect thereto, provided, however, that any and all charges which may be made with respect to drilling expenses and/or accrued income up to the date of acquisition of such properties by Duquesne shall be paid by Kingston.

4. Kingston agrees that it will pay or reimburse to Duquesne the amount of any and all fees and taxes for organization and/or qualification of Duquesne.

In witness whereof, the parties hereto have caused these presents to be executed by their proper officers thereunto duly authorized this 7th day of April, 1930.

Kingston Corporation, By M. H. Furlaud, President.

Attest: Robert Halporn, Assistant Secretary.

Duquesne Gas Corporation, By Walter C. Krog, Vice President.

Attest: Robert Halporn, Assistant Secretary.

[fol. 293] Schedule A

All those certain gas properties particularly described in the following mentioned reports:

1. Report of Ralph E. Davis dated January 27, 1930 on James S. Gallagher properties.

2. Report of Ralph E. Davis dated February 1, 1930 on properties of Trafford Oil & Gas Company, of Campbell & Evans and of Equitable Gas Company.

3. Report of Ralph E. Davis dated January 27, 1930 on properties of Henderson Oil & Gas Company.

4. Report of Mattison, Davey & Winters, dated February 18, 1930 on the five groups of properties therein referred to.

DEFENDANTS' EXHIBIT B

This exhibit consists of the original stock certificate book of Duquesne Gas Corporation.

DEFENDANTS' EXHIBIT C

This exhibit consists of the minute book of the defendant, Kingston Corporation. The said corporation was organized under the laws of the State of New Jersey on March 10, 1926.

[fol. 294] DEFENDANTS' EXHIBIT D

This exhibit consists of a certified copy of the certificate of incorporation of Furlaud & Company, Inc.

Paragraph 3 of the said certificate authorizes Furlaud & Company, Inc. • • •

3. To institute, enter into, conduct, assist in, promote, participate in, invest in, carry on and engage in mining, quarrying, irrigating, agricultural, stock raising, real estate, engineering, contracting, manufacturing, industrial, commercial, mercantile, construction and development enterprises, ventures, operations, contracts, works and businesses of every nature, name and description in any part of the world and so far as permitted by law, within the State of New York.

Paragraph 5 of the said certificate authorizes Furlaud & Company, Inc. • • •

5. To promote and assist financially or otherwise, corporations, firms, syndicates, associations, individuals, and others, and to aid all or any of them by loan, subsidy, guaranty or in any other manner whatsoever.

Paragraph 6 of the said certificate authorizes Furlaud & Company, Inc. • • •

6. To act as financial, commercial, or general agent or representative of any corporation, association, firm, syndicate, individual or others, and as such, to develop, improve [fol. 295] and extend the property, trade and business interests thereof and to aid in lawful enterprises in connection therewith, and in connection with acting as such agent or broker for any principal to give any other aid or assistance to such extent as may be permitted to a corporation organized under said Stock Corporation Law; to undertake and carry on any business, undertaking, enterprise, venture, transaction or operation commonly undertaken or carried on by promoters, contractors, merchants, commission men and agents, and in the course thereof, to acquire and dispose of in any manner whatsoever, and to realize upon, all or any interests in stocks, bonds, debentures, notes, certificates of indebtedness, certificates of interest, commercial paper, mortgages, contracts, choses in action, and any and all kinds of real and personal property.

Defendants' Exhibit E

This exhibit consists of the minutes of a meeting of the corporators and stockholders of Duquesne Gas Corporation, held on February 21, 1930, in Philadelphia, Pennsylvania.

Frank A. Cabeen, Jr., T. Lea Perot, Jr. and B. Raisch, being all of the corporators and stockholders of the company, were present. At that meeting Randolph C. Coleman, McLane Tilton and Frank A. Cabeen, Jr., the directors named in the certificate of incorporation of the Duquesne Gas Corporation, were ratified and confirmed as directors [fol. 296] of company to serve until the next annual election of directors.

The following motion was duly made and seconded and unanimously carried.

Resolved, That the directors of this company be and they hereby are authorized, to issue the capital stock of this company to a total of One thousand (1,000) shares without nominal or par value for money, real or personal property, services rendered, or any of such considerations as they may, from time to time, in their discretion, deem advisable.

Defendants' Exhibit F

Minutes of First Meeting of Directors of Duquesne Gas Corporation

This exhibit consists of the minutes of the meetings of the directors of the Duquesne Gas Corporation.

The first meeting of the directors was held on March 5, 1930 and there were present at that meeting Randolph C. Coleman and McLane Tilton, two of the three directors of the corporation.

The following were elected for the officers set beside their respective names:

Randolph C. Coleman, President; Otto E. Schuller, Vice-President; Charles C. Nuss, Vice-President; Victor D. Behm, Vice-President; Walter C. Krog, Vice-President; [fol. 297] Frank A. Cabeen, Jr., Treasurer; Harry J. Steele, Assistant Treasurer; T. W. D. Duke, Secretary; Robert Halporn, Assistant Secretary; Robert Halporn, Assistant Treasurer.

The following resolution was duly made, seconded and unanimously carried:

Resolved, That the subscriptions of Mr. Frank A. Cabeen, Jr. to 400 shares, of Mr. T. Lea Perot, Jr. to 300 shares and of Miss B. Raisch to 300 shares of the common stock, without par value, of the corporation be, and they hereby are, accepted and the transfers of their subscriptions to Furlaud & Company, Inc. be, and they hereby are, approved and that the proper officers of the corporation be, and they hereby are, authorized and directed to issue and deliver a certificate or certificates of common stock of the corporation to Furlaud & Company, Inc. or its nominee or nominees.

Instructions were received from Furlaud & Company, Inc. to issue a certificate for 997 shares to Furlaud & Company, Inc., a certificate for one share to Frank A. Cabeen, Jr., a certificate for one share to T. Lea Perot, Jr., and a certificate for one share to B. Raisch.

The directors authorized the increase of capital stock from 100 shares of common stock without nominal or par value with a stated capital applicable thereto of Five Hundred Dollars ($500) to 1,250,000 shares of common stock without nominal or par value with a stated capital appli- [fol. 298] cable thereto of Six Hundred and Twenty Five Thousand Dollars ($625,000). The directors also authorized the increase of the indebtedness of the company from nothing to Ten Million Dollars ($10,000,000). A meeting of the stockholders was authorized to be convened on April 3, 1930 to take action of approval or disapproval of the proposed increase of the capital stock and of the indebtedness of the corporation.

Minutes of Special Meeting of Directors of Duquesne Gas Corporation Held on April 7, 1930

There were present Randolph C. Coleman and McLane Tilton being two of the three directors of the corporation.

The following offer was received from Furlaud & Company, Inc.

April 3, 1930.

Duquesne Gas Corporation, Philadelphia, Pa.

GENTLEMEN:

We hereby offer to subscribe to 139,000 additional shares of the common stock of your corporation at the price of

$69,500 cash, or 50c. per share, payable upon the issuance and delivery to us or our nominees of valid certificates evidencing full paid and non-assessable shares of said stock.

Your acceptance hereof as indicated below will constitute [fol. 299] a valid contract between us.

Yours very truly, Furlaud & Company, Inc., by M. H. Furlaud, President.

Accepted:

Duquesne Gas Corporation, Robert Halporn, Assistant Treasurer.

A resolution was passed accepting said offer and authorizing the officers to execute the acceptance at the foot thereof.

The chairman thereupon stated that a plan of financing of the corporation had been developed which contemplated the issuance of First Mortgage Bonds, of General Mortgage Bonds, of notes and of common stock of the corporation in connection with the acquisition of properties and to provide cash for development, expansion and other corporate purposes.

Reports of engineers and Certified Public Accountants who had examined the properties and the books and accounts in connection therewith proposed to be acquired by the corporation were presented to the meeting which reports indicated that the value of the properties proposed to be acquired by the corporation was $6,673,307. These reports were scrutinized and examined by all the directors present.

The following resolution was duly made, seconded and unanimously carried.

Resolved, That all of the acts and resolutions of the stock- [fol. 300] holders at a meeting thereof held on April 3, 1930, as recorded in the minutes of the said meeting presented to this meeting be, and the same hereby are ratified, confirmed and approved.

Thereupon the directors unanimously authorized the proper officers of the company in the name and on behalf of the corporation to execute an indenture of mortgage and note agreement in substantially the forms of the drafts before the meeting and the said officers were further authorized to execute and to cause to be authenticated and

delivered on the order of the corporation $4,000,000 of First Mortgage 6% Convertible Gold Bonds of the corporation, $1,000,000 of General Mortgage 6½% Gold Bonds of the corporation and $1,000,000 of Convertible 6½% Secured Gold Notes of the corporation.

The officers were further directed to deposit with the Pacific Trust Company as Trustee under the said note agreement, $1,000,000 of principal amount of General Mortgage 6½% Gold Bonds of the corporation to secure the payment of the $1,000,000 principal amount of Convertible 6½% Secured Gold Notes of the corporation.

The directors thereupon approved the proposed plan of reorganization between Kingston Corporation and Duquesne Gas Corporation, a copy of which plan was attached to the minutes of the meeting and constitutes Defendant's Exhibit A to which reference is hereby made.

There were presented to this meeting the reports of Messrs. Mattison, Davey & Winters and of Ralph E. Davis, engineers, appraising properties proposed to be transferred by Kingston Corporation to Duquesne Gas Corporation pursuant to the aforesaid plan of reorganization . . $6,673,- [fol. 301] 307 together with a report of Barrow Wade Guthrie & Company, Certified Public Accountants, with respect to the earnings of the said corporation.

The directors unanimously adjudged and declared that in their judgment the value of the properties proposed to be transferred to the Duquesne Gas Corporation under the agreement of reorganization between Kingston Corporation and the Duquesne Gas Corporation was $6,673,307.

The officers of the corporation were further directed, upon the receipt from Kingston Corporation of valid deeds to the properties referred to in the reorganization agreement, to issue to Kingston Corporation or its nominees, certificates for 535,000 shares of common capital stock of the corporation and $1,300,000 principal amount of the First Mortgage 6½% Convertible Gold Bonds.

The following resolution was introduced:

"Further resolved, that the sum of $2,358,307 being the figure remaining after the subtraction from the sum of $6,673,307, representing the valuation of the said properties to be transferred to this Corporation, of the sum of $3,015,- 000, representing the said obligation of the Kingston Corporation to be assumed by this Corporation pursuant to the

said plan of reorganization and of the sum of $1,300,000, representing the principal amount of First Mortgage 6% Convertible Gold Bonds of this Corporation to be issued and delivered to the Kingston Corporation, be and it hereby is determined to be the consideration received by this Corporation for the issuance of the said 535,000 shares of its [fol. 302] common stock without par value."

A proposal from Furlaud & Company, Inc., was read before the meeting and unanimously accepted. The proposal is as follows (Defendant's Exhibit H):

"April 7, 1930.

Duquesne Gas Corporation, Philadelphia, Pennsylvania.

GENTLEMEN:

We hereby offer to purchase from you $2,700,000 principal amount of First Mortgage 6% Convertible Gold Bonds of your Corporation to be issued under an indenture of mortgage dated as of March 15, 1930, between your Corporation and Central Hanover Bank and Trust Company, as Trustee, at the price of 90% of the principal amount thereof, plus accrued interest to the date of purchase, and also purchase from you $1,000,000 principal amount of Convertible 6½% Secured Gold Notes of your Corporation to be issued under a note agreement dated as of March 15, 1930, between your Corporation and Pacific Trust Company, as Trustee, at the price of 88% of the principal amount thereof, plus accrued interest to the date of purchase.

Payment for the said bonds and notes shall be made in funds payable through the New York Clearing House against delivery to us or upon our order of the said bonds [fol. 303] and notes at our office, No. 52 Wall Street, New York City, not later than April 9th, 1930.

It is further understood that our obligation to take and pay for the said bonds and notes is conditioned upon the approval by our counsel of the form, terms and validity of the said bonds and notes and the said indenture of mortgage and note agreement and the validity of all legal proceedings in connection with the creation, authorization and execution of each thereof and the sale of said bonds and notes.

Your acceptance hereof, as indicated below, will constitute the foregoing a valid contract between us.

Yours very truly, Furlaud & Company, Inc., by Carlos Reuter, Vice President.

Accepted:

Duquesne Gas Corporation, by Otto E. Schuller, Vice-President."

The proper officers of the company were directed to issue and deliver to Furlaud & Company, Inc., $2,700,000 principal amount of the First Mortgage 6% Convertible Gold Bonds of the Duquesne Gas Corporation, $1,000,000 of the principal amount of the Convertible 6½% Secured Gold Notes of the Duquesne Gas Corporation, in consideration of the payment in cash of the prices for the said bonds and notes stipulated in the said offer.

[fol. 304] Special Meeting of the Board of Directors of Duquesne Gas Corporation

Held on April 7, 1930, at 10:30 A. M.

A special meeting of the Board of Directors of Duquesne Gas Corporation was held on April 7, 1930, at 10:30 A. M. Randolph C. Coleman and McLean Tilton, being two of the three directors of the company, were present.

It was unanimously resolved to increase the number of the Directors of Duquesne Gas Corporation to six.

The resignations of Messrs. Coleman, Tilton and Cabeen were accepted, to take effect on the termination of the meeting. The following were thereupon elected directors of the company:

M. H. Furlaud, Carlos Reuter, Otto E. Schuller, T. W. D. Duke, H. T. Wynn, Chas. C. Henderson.

Mr. Coleman's resignation as President of the Corporation was accepted, and Mr. Carlos Reuter was elected in his stead.

Mr. Frank A. Cabeen, Jr., resigned as Treasurer of the corporation and Mr. Otto E. Schuller was elected in his stead.

[fol. 305] DEFENDANTS' EXHIBIT G

Minutes of Special Meeting of Stockholders of Duquesne Gas Corporation

Held on April 3, 1930, at 4 P. M.

There were present in person: Mr. Frank A. Cabeen, Jr., T. Lea Perot, Jr., Miss B. Raisch, the holders of three shares of the outstanding Common Stock of the Corporation, and there was represneted by proxy Furlaud & Company, Inc., the holder of 997 shares of the outstanding Common Stock of the Corporation.

The stockholders approved the action of the Board of Directors taken on March 5, 1930, and adopted a resolution increasing the authorized capital stock of the Duquesne Gas Corporation from 1000 shares of Common Stock without nominal or par value, with a stated capital applicable thereto of $500, to 1,250,000 shares of Common Stock without nominal or par value with a stated capital applicable thereto of $625,000.

The stockholders approved a resolution adopted by the Board of Directors on March 5, 1930, and themselves adopted a resolution increasing the authorized indebtedness of the Duquesne Gas Corporation from nothing to Ten million dollars ($10,000,000).

The following resolution was duly made, seconded and unanimously adopted:

"Resolved that all of the acts done and proceedings taken [fol. 306] by the Board of Directors and the officers of this corporation from the date of its organization on February 13, 1930, to the present time, be and the same hereby are in all respects approved, confirmed, ratified and adopted as the valid acts of Duquesne Gas Corporation."

The stockholders authorized the Board of Directors to accept the offer of Furlaud & Company, Inc. to subscribe to 139,000 additional shares of the Common Stock of the Corporation at the price of $69,500 cash, or 50 cents per share.

Upon motion duly made, seconded and unanimously carried, the following preambles and resolutions were adopted:

"Whereas, Duquesne Gas Corporation desires to provide means for the purpose of the acquisition of properties

and for developments, extensions and other corporate purposes; and

"Whereas, the officers of the Corporation have caused to be drafted an indenture of mortgage dated as of March 15, 1930, from the Corporation to Central Hanover Bank and Trust Company, as Trustee, securing $4,000,000 principal amount of First Mortgage 6% Convertible Gold Bonds of the Corporation; and

"Whereas, said indenture of mortgage has been examined by the stockholders of this Corporation now here in meeting assembled and the same found to be suitable and desirable for the accomplishment of the purposes thereof;

[fol. 307] "Now, therefore, be it and it is hereby resolved:

(1) That the Board of Directors of this Corporation be and they hereby are authorized and directed to cause an indenture of mortgage in substantially the form and substance now before this meeting, subject, however, to such changes, additions or amendments as may seem desirable to the proper officers of the Corporation to be signed in the name and on behalf of this Corporation by its President or a Vice President and its corporate seal to be thereunto affixed and attested by its Secretary or an Assistant Secretary and to cause such indenture of mortgage to be delivered to Central Hanover Bank and Trust Company for execution by it as Trustee thereunder;

(2) That the Board of Directors of the Corporation be and they hereby are authorized and directed to cause the corporate officers of the Corporation forthwith upon the execution and delivery of such indenture of mortgage to cause to be executed in the name and on behalf of the Corporation and to be authenticated by Central Hanover Bank and Trust Company, as Trustee, and to be delivered to or upon the order of the President or Vice President of the Corporation, the First Mortgage 6% Convertible Gold Bonds of the Corporation in the aggregate principal amount of $4,000,000 as provided in the said indenture of mortgage;

[fol. 308] (3) That the Board of Directors of the Corporation be and they hereby are authorized and directed to issue and dispose of the said $4,000,000 principal amount of first mortgage bonds secured by the said indenture of

mortgage upon such terms as they in their discretion may deem advisable;

(4) That the Board of Directors be and they hereby are authorized and directed to do all things and to authorize the execution of all contracts, undertakings and agreements necessary or desirable to be done, made or entered into for the purpose of rendering such indenture of mortgage and all bonds proper to be issued thereunder, legal, valid, effective and operative and of making sale of all said bonds proper to be issued under the terms of such indenture of mortgage;

(5) That the form of indenture of mortgage presented at this meeting is in words and figures as follows, to wit:"

A copy of the indenture referred to in the preceding resolutions was annexed to the minutes of the within meeting.

The following portions of the indenture are copied verbatim and are as follows:

At page 5 of the indenture of mortgage securing $4,000,000 principal amount of First Mortgage 6% Convertible Gold Bonds, due March 15, 1945, the following appears:

"No recourse shall be had for the payment of the principal of or the interest upon this bond or of any claim based [fol. 309] hereon or in respect hereof or of said indenture against any past, present or future incorporator, promoter, stockholder, officer or director of the Corporation or of any successor corporation, either directly or through a receiver or trustee in bankruptcy, whether by virtue of any statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability, if any, being, by the acceptance hereof and as part of the consideration for the issue hereof, expressly released, provided that nothing herein shall release any liability arising out of any unlawful abstraction or diminution of the assets of the Corporation."

Further at page 152 of the said indenture of mortgage at Article Thirteen, Section 13.01 thereof, the following paragraph appears:

"The faith and credit of the Corporation are pledged for the payment of the bonds issued hereunder and all interest

thereon, according to the tenor and effect thereof, but each of said bonds is a corporate obligation only, and no recourse whatsoever, either directly or through the Corporation or any trustee, receiver, assignee or any other person, shall be made for the payment of the principal of or interest on any bond, or for the enforcement of any claim based thereon, or otherwise, in respect thereof or of this indenture, or under or upon any obligation, covenant or agreement contained in this indenture, against any promoter, subscriber to the capital stock, incorporator, or any [fol. 310] past, present or future stockholder, officer or director of the Corporation or of any successor or predecessor corporation under any statute or constitution or rule of law or by the enforcement of any assessment, penalty, subscription or otherwise, all such liability of promoters, subscribers, incorporators, stockholders, officers, and directors being waived and released by each successive holder of each bond by the acceptance of such bond and being likewise waived and released by the terms of this indenture provided that nothing herein shall release any liability arising out of any unlawful abstraction or diminution of the assets of the Corporation."

Thereupon the following additional preambles and resolutions were unanimously adopted:

"Whereas, Duquesne Gas Corporation desires to provide additional means for the purpose of the acquisition of properties and to provide cash for developments, extensions and other corporate purposes; and

"Whereas, the officers of the Corporation have caused to be drafted an indenture of general mortgage dated as of March 15, 1930, from Duquesne Gas Corporation to Pacific Trust Company securing $1,000,000 principal amount of General Mortgage 6½% Gold Bonds and have also caused to be drafted an agreement dated as of March 15, 1930, between Duquesne Gas Corporation and Pacific Trust Company, providing for the issuance of $1,000,000 principal [fol. 311] amount of Convertible 6½% Secured Gold Notes to be secured by the pledge with said trustee as collateral of said $1,000,000 principal amount of General Mortgage 6½% Gold Bonds; and

"Whereas, the indenture of general mortgage and said agreement have been examined by the stockholders of the

Corporation now here in meeting assembled and the same found to be suitable and desirable for the accomplishment of the purposes thereof;

"Now, therefore, be it and it is hereby resolved:

(1) That the Board of Directors of the Corporation be and they hereby are authorized and directed to cause an indenture of general mortgage and an agreement, respectively, in substantially the form and substance now before this meeting, subject, however, to such changes, additions or amendments as may seem desirable to the proper officers of the Corporation to be signed in the name of and on behalf of the Corporation by a President or Vice President and its corporate seal to be hereunto affixed and attested by its Secretary or an Assistant Secretary and to cause such indenture of general mortgage and such agreement to be delivered to Pacific Trust Company for execution respectively by it as trustee under each said indenture of general mortgage and agreement;

(2) That the Board of Directors of the Corporation be and they hereby are authorized and directed to cause the [fol. 312] proper officers of the Corporation forthwith upon the execution and delivery of such indenture of general mortgage to cause to be executed in the name of and on behalf of the Corporation and to be authenticated by Pacific Trust Company, as Trustee, and to be held by said Pacific Trust Company as collateral to secure the said $1,000,000 principal amount of Convertible 6½% Secured Gold Notes, the said General Mortgage 6½% Gold Bonds in the aggregate principal amount of $1,000,000 as provided by said indenture of general mortgage;

(3) That the Board of Directors of the Corporation be and they hereby are authorized and directed to issue and dispose of the said $1,000,000 principal amount of Convertible 6½% Secured Gold Notes issued under the said agreement, upon such terms as they in their discretion may deem advisable;

(4) That the Board of Directors be and they hereby are authorized and directed to do all things and to authorize the execution of all contracts, undertakings or agreements necessary or desirable to be done, made or entered into for the purpose of rendering such indenture of general mort-

gage and such agreement and all bonds and notes proper to be issued respectively thereunder, legal, valid, effective and operative and of making sale of all said notes proper to be issued under the terms of such agreement;

[fol. 313] (5) That the forms of indenture of general mortgage and of agreement presented at this meeting are in words and figures respectively as follows, to wit:"

Annexed to the minutes of the within meeting was a copy of the agreement referred to in the said resolutions between the Duquesne Gas Corporation and the Pacific Trust Company dated as of March 15, 1930, securing $1,000,000 Principal Amount of Convertible 6½% Secured Gold Notes.

In the said agreement was set forth the form of note issued pursuant to the said agreement, which note contained as a part thereof the following paragraph:

"No recourse shall be had for the payment of the principal of or the interest upon this note or of any claim based hereon or in respect hereof or of said agreement against any past, present or future incorporator, promoter, stockholder, officer or director of the Corporation or of any successor corporation, either directly or through a receiver or trustee in bankruptcy, whether by virtue of any statute or rule of law or by the enforcement of any assessment or penalty or otherwise, all such liability, if any, being, by the acceptance hereof and as part of the consideration for the issue hereof, expressly released, provided, that nothing herein shall release any liability arising out of any unlawful abstraction or diminution of the assets of the Corporation."

[fol. 314] Section 11.01 of Article Eleven of the said agreement is as follows:

"The faith and credit of the Corporation are pledged for the payment of the notes issued hereunder and all interest thereon, according to the tenor and effect thereof, but each of said notes is a corporate obligation only, and no recourse whatsoever, either directly or through the Corporation or any trustee, receiver, assignee or any other person, shall be had for the payment of the principal of or interest on any note, or for the enforcement of any claim based thereon, or otherwise, in respect thereof or of this agreement, or under or upon any obligation, covenant or agree-

ment contained in this agreement, against any promoter, subscriber to the capital stock, incorporator, or any past, present or future stockholder, officer or director of the Corporation or of any successor or predecessor corporation under any statute or constitution or rule of law or by the enforcement of any assessment, penalty, subscription, or otherwise, all such liability of promoters, subscribers, incorporators, stockholders, officers and directors, being waived and released by each successive holder of each note by the acceptance of such note and being likewise waived and released by the terms of this agreement provided that nothing herein shall release any liability arising out of any unlawful abstraction or diminution of the assets of the Corporation."

[fol. 315] Minutes of Special Meeting of Stockholders of Duquesne Gas Corporation

Held on April 8, 1930

There was represented by proxy Furlaud & Company, Inc. being the holder of 997 shares of the outstanding Common Stock of the Corporation and there were present in person Mr. Frank A. Cabeen, Jr., Mr. T. Lea Perot, Jr. and Miss B. Raisch, the holders of the remaining three shares of the outstanding stock of the Corporation.

The following resolution was unanimously adopted:

"Resolved, that all of the acts done, resolutions adopted and proceedings taken by the Board of Directors and the officers of this Corporation from the date of its organization on February 13, 1930 to the present time be and the same hereby are in all respects approved, confirmed, ratified, and adopted as the valid acts of Duquesne Gas Corporation."

[fol. 316] DEFENDANT'S EXHIBIT H

April 7, 1930.

Duquesne Gas Corporation, Philadelphia, Pennsylvania.

GENTLEMEN:

We hereby offer to purchase from you $2,700,000 principal amount of First Mortgage 6% Convertible Gold

Bonds of your Corporation to be issued under an indenture of mortgage dated as of March 15, 1930, between your Corporation and Central Hanover Bank and Trust Company, as Trustee, at the price of 90% of the principal amount thereof, plus accrued interest to the date of purchase, and also purchase from you $1,000,000 principal amount of Convertible 6½% Secured Gold Notes of your Corporation to be issued under a note agreement dated as of March 15, 1930, between your Corporation and Pacific Trust Company, as Trustee, at the price of 88% of the principal amount thereof, plus accrued interest to the date of purchase.

Payment for the said bonds and notes shall be made in funds payable through the New York Clearing House against delivery to us or upon our order of the said bonds and notes at our office, No. 52 Wall Street, New York City, not later than April 9th, 1930.

It is further understood that our obligation to take and pay for the said bonds and notes is conditioned upon the approval of our counsel of the form, terms and validity of the said bonds and notes and the said indenture of mortgage and note agreement and the validity of all legal proceedings in connection with the creation, authorization [fol. 317] and execution of each thereof and the sale of said bonds and notes.

Your acceptance hereof, as indicated below, will constitute the foregoing a valid contract between us.

Yours very truly, Furlaud & Company, Inc., by Carlos Reuter, Vice-President.

Accepted:

Duquesne Gas Corporation, by Otto E. Schuller, Vice-President.

[fol. 318] IN UNITED STATES DISTRICT COURT

OPINION BY KNOX, D. J.

This is a suit in equity brought by complainant, as Receiver of Duquesne Gas Corporation, to compel defendants to account

"for all funds or moneys coming into the hands of them or or any of them, or of the agents or representatives of any

of them, or in the hands of anyone else acting with or for them, from the sale of the bonds, notes and shares of stock of said Duquesne Gas Corporation."

The special grievance of the bill is that defendants, or some of them, through the instrumentality of an alleged banking house, known as Furlaud & Co., Inc. came into possession of funds arising from the public offerings of securities of Duquesne Gas Corporation, in the relationship of fiduciaries to that company, and that a large portion of the funds so received, were diverted and misappropriated from the treasury of the gas corporation. The defendants named in the bill may be identified as follows:

Maxime H. Furlaud was the president and principal stockholder of Furlaud & Co., Inc. Carlos Reuter, also an officer and large stockholder in Furlaud & Co. Inc., although named as a defendant herein, was not served with process. He is, therefore, out of the case. Kingston Corporation was a wholly owned subsidiary of Furlaud & Co. Inc. Byron Corporation was owned, in part, by the wife of Maxime H. Furlaud, and in part by the Kipling Corporation, the ownership of which was not revealed. Chaucer Corporation was owned partly by the wife of Carlos Reuter, and partly by Vigil Corporation, whose ownership likewise did not appear.

[fol. 319] The evidence discloses that Furlaud & Co. Inc., a New York Corporation, was engaged in the business of selling issues of corporate securities to the public. The series of events under inquiry had its beginning early in 1930 when Reuter went to Pittsburgh, and negotiated with the owners of nine different gas properties located in Western Pennsylvania, for the purchase of their holdings. He secured gratuitous options thereon, which were taken in the name of Kingston Corporation. Ralph E. Davis, an engineer familiar with the value of the properties, was engaged to make an appraisal of the same. Davis, together with a staff of assistants, entered upon the work. By February 1, 1930, he had rendered reports which indicated that five of the properties, including their working capital, had an aggregate value of around $1,700,000. They were subsequently acquired for about $1,300,000. At the time this appraisal was submitted, Davis had about completed his data relating to the four other tracts, and his preliminary figures, as laid before Reuter, showed their approximate

value to be in the neighborhood of $1,000,000. At about this time, Reuter secured possession of Davis's working papers, and retained a Texas concern, by the name of Mattison, Davey & Winters, to complete the appraisal. A man named Conrad, who seems to have had no experience in the Pennsylvania gas fields, was delegated to do the work. After working single-handed for some ten days, Conrad fixed his valuation of the four remaining properties at about five million dollars. Certain of these gas lands which were later conveyed to Duquesne Gas Corporation for $660,000 by one Nuss, who had been born and raised in the field, and who was in the gas business, were valued by Conrad for approxi- [fol. 320] mately $1,900,000. When Nuss made his conveyance, he included therein certain leases upon undeveloped lands which were regarded as a gift. Conrad gave these undeveloped properties a valuation of $850,000. Other lands, known as the Behm properties, the Tucker acreage, and the Levier tract, which were acquired by the gas corporation for a total sum of $222,697, were valued at $1,300,000. From the recital, it will be observed that properties costing about $900,000, were appraised as being worth about $4,000,000. The total appraisal for all of the gas properties examined by Conrad was about $5,000,000 although their total cost was only around $1,200,000.

The valuations thus fixed having been reached near the middle of February, 1930, the bankers procured extensions of their options upon the lands and made payments to the several optioners, upon account of the purchase prices named in the agreements. The documents were enforcible at the election of the optionees.

About a week thereafter, and on February 21, 1930, Furland & Co. Inc. caused Duquesne Gas Corporation to be organized under the laws of the Commonwealth of Pennsylvania. This concern had an authorized capital of 1,000 shares of no par common stock. The stock was subscribed by nominees of Furland & Co. Inc. at fifty cents per share. The banking house then arranged with the several optionors of the gas properties for the execution of deeds of assignment thereon, and for the delivery of the latter and accompanying muniments of title in escrow, to various banks located in Pittsburgh, and its vicinity.

Duquesne Gas Corporation was named as the assignee in the conveyances thus deposited. Under the terms of the

[fol. 321] option agreements, the balance of the purchase price yet to be paid for the properties was $2,449,900, after taking into consideration various down payments which had previously been made by Kingston Corporation.

The next step in the plan under way was the action of Furlaud & Co. Inc. in bringing about the organization of a so-called "Banker's Syndicate," and a distributing group for the sale and distribution to the public of First Mortgage Six Percent Bonds of Duquesne Gas Corporation, of the par value of four million dollars. The Syndicate was headed by Furlaud & Co., Inc. as managers; and included in its membership, were four other so-called banking houses. All were named in the public announcement of the bond issue which appeared in the New York Times of March 25, 1930. Some forty dealers in corporate securities, scattered over the length and breadth of the land, became members of the distributing group. The bonds were offered at 97½ percent of par, and members of the distributing group were entitled to a commission of four percent of par.

At about the time this step was in progress, Duquesne Gas Corporation, the entire capital stock of which was held by Furlaud & Co. Inc. or its nominees, authorized issue of four million dollars of six percent gold bonds, and the one million dollars of 6½ percent notes, to be secured respectively by first and second mortgages upon its properties. The Company's authorized capital was also increased from 1,000 to 675,000 shares, without par value.

Circulars advertising the bonds now made their appearance. These instruments, as well as the announcement that [fol. 322] appeared in the New York Times, proclaimed that the bonds were secured by a mortgage covering properties which, including working capital of $365,000, had an aggregate appraised value of $7,038,000. It was also stated that the properties examined by Mattison, Davey and Winters, had been appraised at $4,929,787, while those examined by Ralph E. Davis, carried an appraisal of $1,743,52[illegible]

There was testimony at the trial that the circulars, as originally printed, combined the appraised values, and indicated that appraisal as having been jointly made by Davis and by Mattison, Davey and Winters. Upon the objection of Davis, this phraseology was changed so as to eliminate such a misrepresentation.

On April 7, 1930, Duquesne Gas Corporation and Kingston Corporation entered into what was termed an "Agreement of Reorganization". This instrument provided that Kingston Corporation would acquire the optioned gas properties then in escrow, and turn them over to Duquesne Gas Corporation. The latter, on its part, agreed to pay $3,015,000 to Central Hanover Bank & Trust Company, the amount which Kingston Corporation would be under obligation to pay to the Trust Company. The Duquesne Company further agreed to issue 535,000 shares of its stock and $1,300,000 face value of its first mortgage six per cent gold bonds to Kingston Corporation, the bonds to be secured by an indenture, dated March 15, 1930, in which the Trust Company was named as Trustee. On April 9, 1930, the following transactions were had at the offices of Central Hanover Bank & Trust Company:

Maxime H. Furlaud arranged with the bank that for a period of one day the Kingston Corporation should have a credit of $3,015,000, and that Furlaud & Company, Inc. for [fol. 323] for a like period of time, should be entitled to a credit of $3,379,500.

When these credits, which were both closely controlled by the Trust Company, had been set up, Kingston Corporation delivered its certified checks, in the aggregate amount of $2,449,900 to the Equitable Trust Company, Guaranty Trust Company of New York and Central Hanover Bank and Trust Company, respectively. These checks were intended to put the drawees in funds with which to meet drafts which had been drawn against them by the banks in Western Pennsylvania, which held in escrow the several instruments of conveyance by which the gas properties were to be transferred to Duquesne Gas Corporation.

The balance which now remained to the credit of Kingston Corporation upon the books of Central Hanover Bank and Trust Company—the sum of $565,100, was immediately paid back to Furlaud & Company, Inc.—$300,000 for alleged loans advanced and expenses incurred, and $265,100 in the form of a loan. This loan, it may be remarked, incidentally, has never been repaid.

The banking institutions which received the checks of Kingston Corporation having made telephonic and telegraphic reports of the payments of the purchase money drafts to the banks holding the escrowed conveyances, the

latter were straightway delivered and recorded. This information, being received, Duquesne Gas Corporation proceeded to issue to Kingston Corporation the 535,000 shares of stock and $1,300,000 face value of bonds which were called for by the agreement of April 7, 1930. Thereupon, Furlaud & Company, Inc. delivered its check to Duquesne Gas Corporation in the sum of $3,379,500. This was sup- [fol. 324] posed to represent the proceeds which the gas corporation was to receive for $2,700,000 par value of its six per cent bonds, its million dollar issue of gold notes, and 139,000 shares of its capital stock. All of these securities were contemporaneously delivered to Furlaud & Company, Inc. and with the credits which thus came into the treasury of Duquesne Gas Corporation, that Company drew its check for $3,015,000 to Central Hanover Bank and Trust Company in payment of the credit that the bank had advanced to Kingston Corporation. Throughout the proceedings, representatives of the various security dealers who were to distribute the bonds to the public were waiting without the room in which the foregoing transactions were being consummated. They carried checks for the purchase price of the bonds which their firms had respectively undertaken to distribute. These checks totaled about $3,000,000 and they were immediately exchanged for about eighty per centum of the whole bond issue. When this had been accomplished, Furlaud & Company, Inc. out of the money so obtained, and with that which had come from Kingston Corporation, liquidated the credit which it had obtained from the Trust Company.

Within a few weeks from the date of closing, Furlaud & Company, Inc. disposed of the balance of the six per cent bonds which had come into its hands. When it had done so, there had been a total realization from their distribution of $3,631,671.04. But this was not all. It was but a few weeks until Furlaud & Company, Inc. sold the million dollar issue of the Gas Company's 6½ per cent notes to the firm of Cullen & Drew for $861,097.69.

[fol. 325] On June 4, 1930, Kingston Corporation recorded a transfer of bonds of Duquesne Gas Corporation in the face value of $1,300,000 to Furlaud & Company, Inc. by way of a dividend in kind. As a matter of fact, however, the bonds had previously been delivered to Furlaud & Company, Inc., and had been sold.

Finally, Kingston Corporation recorded the sale of 85,000 shares of stock of the gas corporation to the Byron Corporation and to the Chaucer Corporation at fifty cents per share. These concerns sold the same for $850,000.

The foregoing transactions may be summarized as follows:

Furlaud & Company, Inc., received $4,492,768.73 from the sale of the bonds and notes. It paid $2,572,989 to the vendors of the gas properties, and turned over $364,500 to Duquesne Gas Corporation. The latter had that sum plus the physical properties and the $500 it had received for its original issue of 1,000 shares of stock; and was obligated upon all of the securities that had been issued. Byron and Chaucer Corporation were in pocket $850,000 and Furlaud & Company, Inc. still had possession of 590,000 shares of the gas corporation stock, as well as cash in the sum of $1,554,779.73.

Upon the proof before the court, there can be but little doubt that the circulars which Furlaud & Company, Inc. issued in connection with the sale and distribution of the bonds and notes of Duquesne Gas Corporation grossly and fraudulently misrepresented the value of the property by which they were secured. The circulars stated that

[fol. 326] "the appraisals of the engineers covering the properties of the corporation, including working capital of $363,000, aggregate $7,038,000."

The manner in which this excessive appraisal was secured has been related. It was accomplished through the simple expedient of displacing a competent and careful engineer with one who either did not know values, or who was willing to lend himself to the promotion of a bond jobbing operation. When, in addition to this procedure, consideration is given to the incontrovertible fact that the cost of the properties, plus $365,000, amounted only to $2,937,989, it is clearly apparent that the value of the properties as given to the public was wantonly misrepresented. Defendants, it may be remarked, offered no evidence to rebut the conclusion that is compelled by plaintiff's proof.

The circulars further stated that the bonds and notes of the gas company were

"issued by the corporation in connection with the acquisition of properties, and to provide cash for developments, extensions and other corporate purposes."

Defendants argue that this statement was true. In a strictly literal sense there is a modicum of justification for the argument. From the standpoint of fair dealing and honest conduct, the statement was utterly false. No stretch of a straight imagination can reconcile its content with the actualities of the situation. What purchasers of bonds and notes would have believed that out of the sum of $4,492,768.73 which they exchanged for the obligations of the [fol. 327] company more than one and one half million dollars would be appropriated by Furlaud & Company, Inc., and that but a trifle less than three million dollars would be devoted to the corporate purposes of the gas corporation?

That the wrong of a misrepresentation may consist of the quality of its concealment rather than in the nature of its revelation, was made abundantly clear by Lord Halsbury in his opinion in the case of Aaron's Reefs v. Twiss, L. R. (App. Cas. 1896), 273, 285, where he said:

"If by a number of statements you intentionally gave a false impression and induce a person to act upon it, it is not the less false although if one takes each statement by itself there may be a difficulty in showing that any specific statement is untrue."

This statement of Lord Halsbury was quoted with approval by the Court of Appeals of this State in Downey v. Finucane, 205 N. Y. 251, 264. In that litigation, as in this, the promoters of a corporation issued a prospectus for the purpose of inducing sales of the corporation's bonds. The circular contained an ambiguous declaration which was interpreted by the promoters to mean that the corporation was obligated to sell bonds in the amount of five million dollars, but that no one was obligated to purchase them. On the trial the jury found that, taking the prospectus as a whole, its language fairly conveyed the impression that contracts had been made which were mutually binding upon the parties thereto under which the corporation was as-[fol. 328] sured of obtaining five million dollars. The Court of Appeals sustained such finding, and held that a general reader would have been misled by the circular. It seems reasonably clear that in the case at bar the purchasers of the bonds and notes of the gas corporation must have been similarly misled. They were induced to part with their

money upon a representation that their payments were to be devoted to the legitimate purposes of the obligor corporation, but they were not apprised that their funds should serve unjustly to enrich the company's promoters.

Had the transaction been characterized by forthright honesty, there would have been no need for the check kiting and other legerdemain that marked the flotation of Duquesne Gas Corporation's securities. All that would have been required had the gas corporation been an independent entity, and a free agency, was that Furlaud & Company, Inc., should have advanced the purchase money of the gas properties, together with a contribution of $364,500 to the company's working capital. In return for this, the corporation could have issued its securities, and Furlaud & Company, Inc. could have done with them as it chose. In place of open and above board procedure, the Kingston Corporation was injected into the situation. This was done for the reason that Furlaud & Company, Inc. intended as it used one hand to pour $3,379,500 into the treasury of the gas corporation, to siphon $565,100 from the treasury with the other. At the end of the complicated series of transactions occurring at the closing, Kingston Corporation was in precisely the same condition as it was at the beginning. Furlaud & Company, Inc. had all the cash over and above [fol. 329] the purchase price of the gas properties, that had come to Kingston Corporation. Furlaud & Company, Inc. also had all of the bonds and notes, and its nominee, Parisette, had all of the gas corporation's corporate stock.

Having come thus far in an analysis of defendant's machinations, it remains to consider if plaintiff in his capacity as a receiver under a creditor's bill and in a foreclosure suit upon the mortgage securing the bonds, has a standing which will here entitle him to relief against those who defrauded not only the purchasers of the corporate bonds and notes but also, the gas corporation itself.

Little time need be spent in arguing the question as to what, under other circumstances, might be the ability of Duquesne Gas Corporation to seek recoupment for the wrong practised upon it, having in mind that such corporation was itself party to the wrong done upon the purchasers of its stocks and bonds. That corporation was the creature of Furlaud & Company, Inc. It, in turn, was dominated, controlled and motivated by Furlaud and

Reuter. At their behest and procurement, the gas corporation acted as it did. It was they who inflicted upon it the congenital injury that stunted its growth and circumscribed its life. In the belief that the money arising from the sale of the bonds and stock of Duquesne Gas Corporation would be utilized in the development and expansion of its prospects and capacity, the purchasers of such securities were induced to part with their money, a substantial portion of which, instead of reaching Duquesne Gas Corporation, was appropriated by Furlaud & Company, Inc.

In McKee v. Lamon, 159 U. S. 317, the Supreme Court, at page 322, said:

"There can be no doubt of the general proposition that [fol. 330] where money is placed in the hands of one person to be delivered to another, a trust arises in favor of the latter, which he may enforce by bill in equity, if not by action at law."

The intention of the giver of the money rather than that of its receiver is determinative of the purpose to which the fund shall be applied. Nor is it essential that the receiver of the fund shall expressly agree that the money be devoted either to a particular purpose, or to a designated third party. The circumstances under which the payments are made may give rise to the existence of a trust duty upon the part of him who recovers the payment. See Sayer v. Winkoop, 248 N. Y. 54. In that case the defendant, an insurance broker, had obtained a policy of Workmen's Compensation insurance in the State Insurance Fund. The insured corporation made two payments of premiums to the broker. The first of these, but not the second, was remitted to the State Fund. Subsequently, the insured corporation became bankrupt, and the receiver of the concern requested defendant to continue the insurance. Five checks, representing premiums upon the policy were sent to defendant. Instead of transmitting the payments to the State Insurance Fund, the defendant cashed the checks and kept their proceeds. The Court of Appeals held that although the broker had made no express promise to pay over the money to the State Fund, he had received the same as a trustee for such purpose, and that as a result, the State Industrial Commission could hold him therefor, in an action for money had and received.

[fol. 331] Upon the facts here present, it would seem that the receipt by Furlaud & Company, Inc., of the money that it received upon the sale of bonds of Duquesne Gas Corporation, and which, under the circulars, was represented as being intended for the use of such corporation, should give rise to a trust in favor of that corporation which may be asserted by its Receiver. If it be said that Duquesne Gas Corporation was party to the fraud practiced upon the purchasers of its bond, the answer to the charge has already been made. It is that misconduct of the gas corporation is chargeable directly to Furlaud & Company, Inc., which motivated, dominated and controlled all of the activities of its supine and acquiescent agent of fraud and deciet. When the gas corporation, at the instance and behest of its master, permitted the latter to retain the sum of $1,554,779.73, it, in effect, made a gift of such sum to Furlaud & Company, Inc. It had no license or authority, as against its note and bondholders, so to dispose of their money. While the disposition that was made of the money was in no sense a secret to Duquesne Gas Corporation, it was, in reality, a secret profit to Furlaud & Company, Inc. In other words, that corporation concealed pertinent facts from the persons who purchased bonds and notes in reliance upon the circulars in which the securities of Duquesne Gas Corporation were offered for sale. In a sense, the situation is analogous to those in which promoters have been held liable for profits accruing to themselves through the misrepresentation of the true value of property conveyed to a corporation, when reliance upon such misrepresentation has been had by innocent purchasers of the stock of the corporation. See Davis v. Las Ovas Company, 227 U. S. 80; [fol. 332] Walker v. Pike Co. Land Co., 139 Fed. 609; cf. Gates v. Megargel, 266 Fed. 811 (C. C. A. 2nd). It is difficult to see how, if at all, the action of Furlaud & Company, Inc., is a whit less reprehensible than the acts of the promoters in the cases just cited.

In considering the right of the Receiver of Duquesne Gas Corporation to maintain this suit, it must be remembered that the receiver represents not only the corporations, but all those having an interest in its properties as well. See Atlantic Trust Company v. Chapman, 208 U. S. 360, 371; Graselli Chemical Company v. Aetna Explosive Company, 252 Fed. 456 (C. C. A. 2nd). To employ the language of the

court in Westinghouse Electric & Manufacturing Company v. Binghamton Railway Company, 253 Fed. 378, at page 385, it may be said that

"a receivership is for the benefit and protection of all interests, general creditors, secured creditors (bondholders) and stockholders, and it is the duty of the court, so far as reasonably possible, to conserve and protect all inte ts."

It has frequently been held that a receiver can disaffirm fraudulent contracts and conveyances which the corporation could not disaffirm, and also, that the receiver can recover for the wrong that has been wrought upon the creditors. Hamor v. Taylor Rice Engineering Company, 84 Fed. 392; Pittsburgh Carbon Company v. McMillin, 119 N. Y. 46; See Thompson on Corporations, 3rd Ed., Sec. 6436; Smith, Law and Procedure of Receivers, 2nd Ed., Section 357. Although it may be that Duquesne Gas Corporation might not be able, in its own right, to hold Furlaud & [fol. 333] Company, Inc., and its masters to accountability for the fraud that was here worked, simple justice requires that the receiver, in his representative capacity, should be able to vindicate the rights of creditors who were victimized. If a court of equity is to function within the domains of conscience, and if it is to redress the wrongs that occur within that dominion, it must provide a remedy that is capable of checkmating the ingenuity that here perpetrated a grievous wrong.

At this point, it may not be amiss to record the genealogy of Furlaud & Company, Inc. Originally incorporated under that name on July 18, 1928, it became known as Furlaud, Reuter & Company, Inc., on August 1, 1930. Upon October 10, 1931, that name was changed to Winchelsea Holding Corporation. Seventeen days later it was dissolved. Throughout the period of its existence, Maxime H. Furlaud, as has been told, was a director, president and principal stockholder of the concern. Also, as has been related, he was a participant in all that gave rise to this suit, and possessed full knowledge thereof. As the guiding spirit, and conscious participant in the wrongs that were done, he incurred liability to the receiver for the ..ust funds which be diverted from the corporation. Anderson v. Daley, 38 A. D. 505, appeal dismissed, 149 N. Y. 146. In that case, one Daley was a bookkeeper, stockholder, officer and di-

rector of Devlin & Company, a business corporation. As trustee under the Will of Albert Ward he deposited moneys of the Ward Estate with the corporation, which subsequently became insolvent. In the meantime, one Jones, another director of Devlin & Company, died, and the bene- [fol. 334] ficiaries of the Ward Estate brought action to charge the Jones Estate with the balance due to the Ward Estate by the corporation. The Court held that they could recover, saying—

"It (the proof) does, however, clearly establish that Jones was aware of the insolvent condition of the corporation, and he also had knowledge that moneys of the estate were being furnished by the trustee and used in the business of the corporation. He was an active participant in the use of such moneys. * * * the evidence is clearly sufficient to charge him with knowledge and participation in their use for the business of the corporation, and therefore, for his own benefit; and this is sufficient to charge him with liability. * * * *Nor can he shield himself by the fact that in what he did he acted as an officer of the corporation. The corporation could only act through its officers, and it is not essential that the misuse of the trust funds should be for the exclusive benefit of the person making such unlawful use, or indeed any benefit at all. Where he possesses the knowledge of the misuse of the trust funds, and knowingly applies them either for his own benefit or for the benefit of another, his liability is complete, as the injury to the estate is the same whether he do it as an officer or as an individual. The basis of his liability is knowledge and injury, both of which here exist.*" (Italics mine.)

[fol. 335] In Virginia-Carolina Chemical Company v. Ehrich, 230 Fed. 1005, it was held that a suit to charge the officers and directors of a corporation with personal liability for the misappropriation by the corporation of money held by it as trustee, was properly brought in equity, upon the theory that the directors were under a duty to exercise reasonable care to supervise the activities of the corporation. The plaintiff, in fact, failed to prove neglect of duty on the part of the defendants in that case, but the implication was clear that they would have been held liable if such neglect had been proven.

The present suit presents a much stronger case for the imposition of liability upon the defendant Furlaud than either of these two cases. The evidence here shows much more than neglect of duty as a director; it shows active participation by the directing personality of the corporation in the transactions which resulted in a misappropriation of money received in trust. Under the foregoing decision, his personal liability is clear.

The defendant, Kingston Corporation, is under a liability for similar reasons. It took part in every step of the proceedings. It received bonds from Duquesne Gas Corporation and turned them over to Furlaud & Company, Inc., without receiving any consideration therefor. It made a gift to Furlaud & Company, Inc., of the $565,100, which it had received as part of its consideration for transferring the various gas properties to Duquesne Gas Corporation. It thus knowingly acted as a conduit through which Furlaud & Company, Inc., its sole stockholder, was enabled to appropriate to its own use money intended to be paid over to Duquesne Gas Corporation. As an agent of Furlaud & Company, Inc., that participated in the commission of a [fol. 336] breach of trust, it is severally liable to account for the sums diverted. Cf. Iroquois Iron Company v. Kruse, 241 Fed. 433.

The defendants, Byron and Chaucer Corporation, however, are under no liability with respect to the issuance of the bonds and notes since they had no part in any of the transactions through which the trust funds were appropriated.

So far I have dealt only with the profits realized from the sale of the bonds and notes. Plaintiffs also urge that the defendants should be required to account for the profits in the sum of $850,000 which were received by Byron and Chaucer Corporations from the sale of 85,000 shares of the stock of Duquesne Gas Corporation to J. J. Bergen, a dealer in stocks. This stock, although originally issued in the name of Parisette, Furlaud & Company's nominee, was subsequently transferred to Kingston Corporation, which in turn transferred it to Byron and Chaucer Corporations. At the time that the transactions through which Duquesne Gas Corporation acquired the various gas properties were consummated, and for some time thereafter, Furlaud & Company, Inc., owned every share of its capital stock, and

ratified and approved of the whole transaction. However much the persons who subsequently purchased stock from Byron and Chaucer Corporations may have been injured, it does not seem that the receiver can recover on behalf of Duquesne Gas Corporation, under the doctrine announced in the case of Old Dominion Copper Company v. Lewishon, 210 U. S. 206. Nor can he recover, as in the case of the bonds and notes, on the theory that the money paid in by purchasers of stock became impressed with a trust in favor of the corporation. This is so for the reason that the evi- [fol. 337] dence does not show that any representation was made, by circulars or otherwise, that the money so received would be paid over to Duquesne Gas Corporation. The complaint, therefore, will be dismissed as against the defendants, Byron Corporation and Chaucer Corporation.

Plaintiff may have a final decree against the defendants, Maxime H. Furlaud and Kingston Corporation. There is no necessity for the expense and delay of a lengthy accounting proceeding before a Special Master. Upon the evidence before the court, it is clear that the amount of trust money diverted from Duquesne Gas Corporation was $1,554,779.73; the difference between the $4,492,768.73 realized by Furlaud & Company from the sale of the bonds and notes, and the $2,937,989.00 actually devoted to the legitimate corporate purposes of Duquesne Gas Corporation. There is no occasion to determine any offset to this amount by way of expenses incurred, or reasonable compensation to Furlaud & Company for its activities in connection with the sale of the securities. A trustee is not entitled to be reimbursed for any money which he expends in the course of defrauding his beneficiary. Commonwealth Finance Corporation v. McHarg, 282 Fed. 560 (C. C. A. 2nd).

Decree for Plaintiff against the defendants, Maxime H. Furlaud and Kingston Corporation in the sum of $1,554,779.73.

April 14, 1933.

Jno. C. Knox, U. S. D. J.

[fol. 338] IN UNITED STATES DISTRICT COURT

[Title omitted]

ORDER BY KNOX, D. J.—May 11, 1933

This cause having come on to be heard before the Honorable John C. Knox, one of the Judges of the United States District Court for the Southern District of New York on the 9th day of November, 1932, and this case having been argued by counsel, testimony and proof having been introduced and the Court having handed down its opinion dated the 14th day of April, 1933, it is hereby

Ordered, adjudged and decreed that the opinion heretofore filed on the 14th day of April, 1933, stand as the findings of fact and conclusions of law in this case and be deemed to constitute the formal decision thereof.

Jno. C. Knox, U. S. D. J.

[fol. 339] IN UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK

E-66-185

GEORGE W. MCCANDLESS, as Receiver of Duquesne Gas Corporation, Complainant,

vs.

MAXIME H. FURLAUD, CARLOS BEUTER, KINGSTON CORPORATION, BYRON CORPORATION and CHAUCER CORPORATION, Defendants

FINAL DECREE

This cause came on to be heard at this term, and was argued by counsel; and thereupon, upon consideration thereof, this Court being duly advised in the premises, it is

Ordered, adjudged and decreed, that complainant George W. McCandless, as Receiver of Duquesne Gas Corporation, do have and recover of and from defendants Maxime H. Furlaud and Kingston Corporation, and each of them, the sum of One million, eight hundred thirty four thousand, six hundred forty and 8/100 Dollars ($1,834,640.08), being the

amount (including interest to this date) found by the Court to be owing by said defendants to the complainant on an accounting of the matters referred to in the complaint with interest thereon at the rate of six per cent. (6%) per an-
[fol. 340] num from this date, together with his costs and disbursements herein, for which let execution issue, and it is

Ordered, adjudged and decreed, that the bill of complaint herein be and the same hereby is dismissed as to defendants Byron Corporation and Chaucer Corporation on the merits without costs.

Dated, New York City, May 11, 1933.

Jno. C. Knox, U. S. D. J.

[fol. 341] In United States District Court, Southern District of New York

[Title omitted]

Defendants' Notice of Appeal and Order Allowing Appeal

To the Hon. the Judges of the District Court of the United States for the Southern District of New York:

Please take notice that the above named defendants, Maxime H. Furlaud and Kingston Corporation, feeling aggrieved by the decree in the above entitled action, dated the 11th day of May, 1933 and filed in the office of the Clerk of the United States District Court for the Southern District of New York on the 12th day of May, 1933, and entered as a judgment in the said Clerk's Office on the 15th day of May, 1933, and feeling aggrieved by an order made and filed in the office of the Clerk of the United States District Court for the Southern District of New York on the 23rd day of June, 1932, denying the motion of the defendants
[fol. 342] Maxime H. Furlaud and Kingston Corporation to require the complainant to make a further and better statement of the nature of the claim and/or claims set forth in the amended bill of complaint herein, do hereby appeal from the said decree and/or decrees to the Circuit Court of Appeals for the Second Circuit for the reasons set forth in the assignment of errors filed herewith, and the defend-

ants Maxime H. Furlaud and Kingston Corporation pray that the appeal herein be allowed and that citation be issued as provided by law and that a transcript of the record, proceedings and documents upon which the said decree and/or order were based duly authenticated, be sent to the United States Circuit Court of Appeals for the Second Circuit, sitting at New York, N. Y., under the rules of said Court in such cases made and provided.

Dated, New York, July 19th, 1933.

Eppstein & Hirshfield, Solicitors for Defendants Maxime H. Furlaud and Kingston Corporation, Office & P. O. Address, 521 Fifth Avenue, Borough of Manhattan, City of New York, N. Y.

Appeal allowed this 19th day of July, 1933.

Wm. Bondy, U. S. D. J.

[fol. 343] In United States District Court, Southern District of New York

[Title omitted]

Statement as to Bond

An undertaking dated July 14th, 1933 by the Glens Falls Indemnity Co. in the sum of $250 for the payment of costs was approved by the Hon. William Bondy, one of the Justices of the United States District Court for the Southern District of New York on the 20th day of July, 1933 and filed on that date.

The printing of such bond is dispensed with by consent.

[fol. 344] In United States District Court, Southern District of New York

[Title omitted]

Defendants' Assignments of Error

Now come the appellants, Maxime H. Furlaud and Kingston Corporation, by Eppstein & Hirshfield, their solicitors, and in connection with their petition for appeal say that in

the record, proceedings and in the final decree aforesaid, manifest error has intervened to the prejudice of the appellants, to wit:

1. The Court erred in holding that the complainant above designated was a proper party to bring the within suit.

2. The Court erred in holding that the order dated March 23, 1932, signed by Hon. Wm. Bondy in the action entitled "Frank T. Harrington, Complainant, against Duquesne Gas Corporation, Defendant", instituted in the Southern District of New York, constituted a due or valid appointment of George W. McCandless as ancillary receiver of the [fol. 345] Duquesne Gas Corporation in the Southern District of New York, or that the complainant had otherwise been duly appointed ancillary receiver.

3. The Court erred in holding that the Duquesne Gas Corporation or complainant had any claim or alleged claim or cause of action that could be asserted or enforced against the defendants Maxime H. Furlaud and Kingston Corporation or against Furlaud & Company, Inc.

4. The Court erred in not holding that the complainant represented only the Duquesne Gas Corporation, and could enforce only the claims and/or rights which that corporation had if any, against the defendants.

5. The Court erred in holding that the complainant, as Receiver of Duquesne Gas Corporation, could enforce any claims or rights which purchasers and/or holders of the bonds or notes of the Duquesne Gas Corporation had or may have had against the defendants Furlaud and Kingston Corporation and/or against Furlaud & Company, Inc.

6. The Court erred in holding that the complainant, as Receiver of Duquesne Gas Corporation, could assert any claim against the defendant Furlaud or the defendant Kingston Corporation or against Furlaud & Company, Inc. and could recover from the defendants Maxime H. Furlaud and Kingston Corporation on account of any transaction which the said parties had with Duquesne Gas Corporation or with each other as a result of which they acquired the bonds and/or the notes of the Duquesne Gas Corporation.

[fol. 346] 7. The Court erred in not holding that any alleged claim asserted by the complainant herein could be enforced, if at all, only in a suit, brought by individual bondholders and/or noteholders.

8. The Court erred in not holding that under the terms of the bonds of the Duquesne Gas Corporation and the indenture of mortgage securing the said bonds, no recourse could be had against the defendants herein for the payment of any claim or alleged claim based upon any bond of the Duquesne Gas Corporation.

9. The Court erred in not holding that under the terms of the notes of the Duquesne Gas Corporation and the agreement securing the said notes, no recourse could be had against the defendants herein for the payment of any claim or alleged claim based upon any note of the Duquesne Gas Corporation.

10. The Court erred in receiving any testimony relating to the value of the properties acquired by the Duquesne Gas Corporation or relating to any claimed over-valuation or erroneous appraisals of the said properties. The testimony referred to in this particular assignment of error was elicited from the plaintiff's witnesses Charles C. Nuss, Walter C. Krog, Lyon F. Terry and Cyrus C. Robbins.

11. The Court erred in holding as a matter of law that there was any competent testimony as to any claimed over-valuation of the properties acquired by the Duquesne Gas Corporation or that the appraisals of the said properties were erroneous or fraudulent.

[fol. 347] 12. The Court erred in ruling that the witness Charles C. Nuss was competent to testify as to the value of the oil and gas properties acquired by the Duquesne Gas Corporation.

13. The Court erred in holding that certain leases upon undeveloped lands were transferred by Nuss to the Duquesne Gas Corporation as a gift.

14. The Court erred in finding that $565,100 represented the balance which remained to the credit of the defendant Kingston Corporation upon the books of the Central Hanover Bank & Trust Company after Kingston Corporation

had made payments with respect to the properties transferred to Duquesne Gas Corporation.

15. The Court erred in finding that the loan of $265,100 made by the defendant Kingston Corporation to Furlaud & Company, Inc. has never been repaid.

16. The Court erred in finding that the checks presented at the closing on April 9, 1930, by representatives of the various security dealers who were to distribute the Duquesne Gas Corporation bonds to the public totalled about $3,000,000.

17. The Court erred in failing to find that the checks presented on April 9, 1930, at the closing by various security dealers totalled $1,866,330.

18. The Court erred in finding that the checks presented on April 9, 1930, by the represenatives of the various security dealers at the closing were immediately exchanged for about 80 per cent of the whole bond issue.

[fol. 348] 19. The Court erred in not finding that on the 9th day of April, 1930, only $2,500,000 par value of the bonds of the Duquesne Gas Corporation were taken up by the security dealers.

20. The Court erred in finding that Furlaud & Company, Inc. liquidated the loan which it had obtained from the Central Hanover Bank & Trust Company only by the application of the money obtained from the various security dealers together with the money which had come from Kingston Corporation.

21. The Court erred in failing to find that Furlaud & Company, Inc. liquidated the loan which it had obtained from the Central Hanover Bank & Trust Company by the application (1) of the moneys which it had obtained on that day from the various security dealers who had purchased the Duquesne Gas Corporation bonds from Furlaud & Company, Inc. and (2) of the sum of $1,500,000 which it had borrowed from the Hibernia Trust Company, Chatham & Phenix National Bank & Trust Company, and the Pacific Trust Company.

22. The Court erred in finding that the sum of money realized by Furlaud & Company, Inc. from the distribution

of the Duquesne Gas Corporation 6 per cent Bonds was $3,631,671.04.

23. The Court erred in finding that Furlaud & Company sold $1,000,000 par value of Duquesne Gas Corporation 6½ per cent notes to the firm of Cullen & Drew for $861,097.69.

24. The Court erred in finding that the $1,300,000 face value of Duquesne Gas Corporation Bonds delivered by [fol. 349] Kingston Corporation to Furlaud & Company, Inc. by way of a dividend in kind, declared on June 4, 1930, had previously been delivered to Furlaud & Company, Inc. and had been sold.

25. The Court erred in finding that Furlaud & Company, Inc. received $4,492,768.73 from the sale of the bonds and notes of the Duquesne Gas Corporation.

26. The Court erred in finding that Furlaud & Company, Inc. paid $2,572,989 or any sum whatsoever to the vendors of the gas properties acquired by the Duquesne Gas Corporation.

27. The Court erred in holding that there was any competent evidence or any facts presented which would justify a finding that any alleged misrepresentation was made by Furlaud & Company, Inc. or the defendants or any one in connection with the sale and distribution of the securities of the Duquesne Gas Corporation.

28. The Court erred in holding that the circulars issued in connection with the sale and distribution of the bonds and notes of Duquesne Gas Corporation grossly and fraudulently misrepresented the value of the property by which they were secured.

29. The Court erred in holding that the statement in the circulars that the bonds and notes of the Duquesne Gas Corporation "were issued by the corporation in connection with the acquisition of properties, and to provide cash for developments, extensions, and other corporate purposes" [fol. 350] constituted a misrepresentation and was utterly false.

30. The Court erred in holding that there was any duty on the part of Furlaud & Company, Inc. or of any of the

defendants to inform the purchasers of bonds or notes what portion of the sums paid for the bonds or notes would be devoted to the corporate purposes of the Duquesne Gas Corporation and what portion would be retained by Furlaud & Company, Inc.

31. The Court erred in holding that the defendants or any of them issued a circular covering the sale of the notes of the Duquesne Gas Corporation.

32. The Court erred in holding that any one was induced to purchase a bond or a note of the Duquesne Gas Corporation by any representation or misrepresentation made either by Furlaud & Company, Inc. or by any of the defendants or by any one whatsoever.

33. The Court erred in holding that there was any duty upon the defendants and/or Furlaud & Company, Inc. to devote any monies received by them from the sale of the bonds or notes of the Duquesne Gas Corporation for the benefit or to the purposes of the said corporation.

34. The Court erred in holding that any representation or misrepresentation made by Furlaud & Company, Inc. to purchasers of the bonds and notes of the Duquesne Gas Corporation created any right or interest in the said corporation in the proceeds derived from the sale of the said securities.

[fol. 351] 35. The Court erred in holding that any funds or property which the Duquesne Gas Corporation was entitled to receive or in which it had any interest were diverted from it by Furlaud & Company, Inc. or by any of these defendants.

36. The Court erred in finding that the defendant Kingston Corporation was used for fraudulent purposes in connection with the acquisition of the properties of the Duquesne Gas Corporation and the sale of its securities.

37. The Court erred in holding that the Duquesne Gas Corporation was party to any alleged wrong committed upon the purchasers of its securities.

38. The Court erred in holding that there were any circumstances surrounding the payments made to Furlaud & Company, Inc. by the purchasers of the securities of the Duquesne Gas Corporation, which gave rise to a trust duty

on the part of Furlaud & Company, Inc. or the defendants or both toward the said purchasers or toward the Duquesne Gas Corporation.

39. The Court erred in finding that the Duquesne Gas Corporation permitted Furlaud & Company, Inc. to unlawfully retain the sum of $1,554,779.73 or any sum whatsoever or that Furlaud & Company, Inc. received a secret profit to that extent.

40. The Court erred in holding as a matter of law that the situation in the case at bar is analogous to those situations in which promoters have been held liable for profits [fol. 352] accruing to themselves through the misrepresentation of the true value of property conveyed to a corporation, when reliance upon such misrepresentation has been had by innocent purchasers of the stock of the corporation.

41. The Court erred in finding that the defendant Maxime H. Furlaud was the guiding spirit and conscious participant in the wrongs that are claimed to have been done in connection with the acquisition of the properties of the Duquesne Gas Corporation and the sale and distribution of its securities and possessed full knowledge thereof.

42. The Court erred in holding as a matter of law that the defendant Maxime H. Furlaud incurred liability to the Receiver of the Duquesne Gas Corporation for alleged trust funds claimed to have been diverted from the Duquesne Gas Corporation.

43. The Court erred in holding as a matter of law that the defendant Maxime H. Furlaud was personally responsible for any misappropriations of the funds of the Duquesne Gas Corporation claimed to have been made by Furlaud & Company, Inc.

44. The Court erred as a matter of law in holding that the defendant Kingston Corporation was liable for the claimed misappropriations.

45. The Court erred in finding that the defendant Kingston Corporation delivered bonds of the Duquesne Gas Corporation to Furlaud & Company, Inc. without receiving any consideration therefor.

[fol. 353] 46. The Court erred in finding that the defendant Kingston Corporation made a gift to Furlaud & Company, Inc. of $565,100, or of any sum whatsoever.

47. The Court erred in holding that the defendant Kingston Corporation acted as a conduit or agent through which Furlaud & Company, Inc. was enabled to appropriate to its own use money intended to be paid over to Duquesne Gas Corporation.

48. The Court erred in holding as a matter of law that the defendant Kingston Corporation and the defendant Maxime H. Furlaud were liable to account to the complainant for any sums claimed to have been diverted from the Duquesne Gas Corporation.

49. The Court erred in decreeing that the complainant recover of the defendants Maxime H. Furlaud and Kingston Corporation the sum of $1,834,640.08 or any amount whatsoever.

50. The Court erred in holding that there was no necessity for an accounting and in failing and in refusing to submit the matter to a master to take an account.

51. The Court erred in permitting complainant's witness, Roger A. McShea, Jr., to testify concerning the results of his examination of the books of Furlaud & Company Inc.

52. The Court erred in denying defendants' motion to strike out the testimony of the complainant's witness Roger A. McShea, Jr.

[fol. 354] 53. The Court erred in holding that the alleged trustees, the defendants herein, are not entitled to have offset against the amount awarded to the complainant, all monies expended and expenses incurred by Furlaud & Company, Inc. in connection with its activities in the acquisition of the properties owned by the Duquesne Gas Corporation and in the sale of the bonds and notes of the Duquesne Gas Corporation together with reasonable compensation for the services it rendered in connection therewith.

54. The Court erred in denying the motion made on behalf of the defendants Maxime H. Furlaud and Kingston Corporation to dismiss the amended complaint at the close of the entire case.

55. The Court erred in not dismissing the Plaintiff's Bill for want of equity.

56. The Court erred in entertaining the within suit in equity in violation of Section 267 of the Judicial Code (28 U. S. C. A. Sec. 384).

57. The Court erred in retaining the within suit in equity in violation of Rule 22 of the Equity Rules and in violation of the defendants' right to trial by jury preserved under the Seventh Amendment to the United States Constitution.

58. The United States District Court for the Southern District of New York erred in denying, by an order dated June 23, 1932, the applications made by the defendants herein by orders to show cause dated May 19, 1932, to require the complainant to make a further and better statement of [fol. 355] the nature of the claim and/or claims set forth in the amended bill of complaint herein.

59. The Court erred in receiving any testimony with regard to the appraisals and valuation of the properties acquired by the Duquesne Gas Corporation as binding on the defendant Maxime H. Furlaud.

60. The Court erred in receiving any testimony herein with regard to the issuance of the circulars and the representations contained therein as binding upon the defendant Maxime H. Furlaud.

61. The Court erred in admitting the following exhibits in evidence as binding on the defendant Maxime H. Furlaud—Plaintiff's Exhibit 2 to 31 inclusive.

62. The Court erred in not holding that there was a fatal variance between the allegations of the amended bill of complaint and the proof herein and in not dismissing the amended bill therefor.

63. The decree is against the weight of the evidence.

64. The decree is contrary to law.

65. There are other plain errors of the Court apparent on the face of the record not hereinbefore specifically assigned.

Wherefore the appellants pray that the decree of the District Court of the United States for the Southern Dis-

[fol. 356] trict of New York, dated the 11th day of May, 1933, may be reversed and the amended complaint herein be dismissed.

Dated, New York, July 19th, 1933.

Eppstein & Hirshfield, Solicitors for Defendants-Appellants Maxime H. Furlaud and Kingston Corporation.

To: Charles Weiser, Esq., Clerk of the United States District Court.

Ehrich, Royall, Wheeler & Walter, Esqs., Solicitors for Complainant, 20 Exchange Place, New York, N. Y.

[fol. 357] Citation in usual form omitted in printing.

[fol. 358] In United States District Court, Southern District of New York

[Title omitted]

Complainant's Petition on Appeal and Order Allowing Appeal

The complainant, George W. McCandless, as receiver of Duquesne Gas Corporation, feeling himself aggrieved by that part of the decree in the above entitled suit, dated May 11, 1933, filed in the office of the Clerk of the United States District Court for the Southern District of New York on May 12, 1933 and entered as a judgment in said Clerk's office on May 15, 1933, which dismisses the bill of complaint as to defendants Byron Corporation and Chaucer Corporation on the merits and fails to give judgment against said defendants Byron Corporation and Chaucer Corporation as well as against defendants Maxime H. Furlaud and Kingston Corporation for $850,000 received from the sale of Duquesne Gas Corporation stock with interest thereon, does hereby appeal from all that part of said decree to the Circuit Court of Appeals for the Second Circuit for the reasons set forth [fol. 359] in the assignment of errors filed herewith and he prays that this appeal may be allowed, that a citation be issued directed to the above named defendants Byron Cor-

poration, Chaucer Corporation, Maxime H. Furlaud and Kingston Corporation, as provided by law and that a transcript of the record, proceedings and papers upon which said decree was made be duly authenticated and sent to the United States Circuit Court of Appeals for the Second Circuit sitting at New York, N. Y., under the rules of said Court.

Dated, New York City, August 9, 1933.

Ehrich, Royall, Wheeler & Walter, Solicitors for Complainant, Office and P. O. Address, No. 20 Exchange Place, Borough of Manhattan, City of New York.

Appeal allowed this 10th day of August, 1933.

Robert P. Patterson, U. S. D. J.

[fol. 360] In United States District Court, Southern District of New York

[Title omitted]

Statement as to Bond

An undertaking dated July 31, 1933, by the American Surety Co. in the sum of $250. for the payment of costs was approved by the Hon. Robert P. Patterson, one of the Justices of the United States District Court for the Southern District of New York on the 10th day of August, 1933 and filed on that date. The printing of said bond is dispensed with on consent.

[fol. 361] In United States District Court, Southern District of New York

[Title omitted]

Complainant's Assignment of Errors

Now comes the appellant, George W. McCandless as receiver of Duquesne Gas Corporation, by Ehrich, Royall, Wheeler & Walter, his solicitors, and in connection with his appeal assigns the following errors in the findings of fact and conclusions of law and in the final decree of this Court, dated May 11, 1933, entered in the office of the Clerk of the

United States District Court for the Southern District of New York on May 12, 1933, and docketed as a judgment in said Clerk's office on May 15, 1933:

First: The Court erred in holding that complainant, as receiver of Duquesne Gas Corporation, had no claim which could be asserted against defendants Furlaud, Reuter, Byron Corporation and Chaucer Corporation arising from the sale of 85,000 shares of the capital stock of Duquesne Gas Corporation for the sum of $850,000.

[fol. 362] Second: The Court erred in not giving judgment to Complainant for $425,000 against defendant Byron Corporation and $425,000 against defendant Chaucer Corporation with interest thereon.

Third: The Court erred in not finding that defendants Maxime H. Furlaud and Kingston Corporation were responsible for the acts of defendants Byron Corporation and Chaucer Corporation in acquiring said shares without consideration being paid therefor to Duquesne Gas Corporation.

Fourth: The Court erred in not finding that defendants Maxime H. Furlaud and Kingston Corporation were accountable to complainant for the $850,000 received by defendants Byron Corporation and Chaucer Corporation from the sale of said shares.

Fifth: The Court erred in not giving judgment to complainant against defendants Maxime H. Furlaud and Kingston Corporation for the $850,000 received by defendants Byron Corporation and Chaucer Corporation from the sale of stock of Duquesne Gas Corporation with interest upon said sum of $850,000, in addition to the amount of $1,834,640.08 awarded in the judgment granted.

Wherefore, the appellant prays that so much of the decree of the United States District Court for the Southern District of New York, dated May 11, 1933, as dismisses the bill of complaint as to the defendants Byron Corporation and Chaucer Corporation and fails to give complainant judgment against defendants Maxime H. Furlaud and Kingston Corporation for the $850,000 received from the sale [fol. 363] of stock, in addition to the amount of $1,834,640.08 awarded in the judgment granted, may be modified and

judgment given against defendants Byron Corporation and Chaucer Corporation for $425,000 each and against Maxime H. Furlaud and Kingston Corporation for an additional $850,000 each, with interest.

Dated New York City, August 9, 1933.

Ehrich, Royall, Wheeler & Walter, Solicitors for Complainant-Appellant. Office & P. O. address: No. 20 Exchange Place, Borough of Manhattan, City of New York.

To Charles Weiser, Esq., Clerk of the United States District Court.

Eppstein & Hirshfield, Esqs., Solicitors for Defendants Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, 521 Fifth Avenue, New York City.

[fols. 364 & 365] Citation directed to Byron Corporation, Chaucer Corporation, Maxime H. Furlaud and Kingston Corporation omitted in printing.

[fol. 366] In United States District Court, Southern District of New York

[Title omitted]

Order Extending Term Until October 6, 1933 (Kingston Corporation and Maxime H. Furlaud)

Upon the annexed stipulation, it is, now on motion of Eppstein & Hirshfield, solicitors for the defendants-appellants-appellees, Maxime H. Furlaud and Kingston Corporation,

Ordered that the time for the defendants-appellants-appellees, Maxime H. Furlaud and Kingston Corporation to serve and file the record on appeal in the above matter in the office of the Clerk of the United States Circuit Court of Appeals for the Second Circuit, be and the same hereby is extended up to and including the 6th day of October, 1933.

Dated New York, September 25, 1933.

Charles Weiser, Clerk of the United States District Court, Southern District of New York.

[fol. 367] In United States District Court

[Title omitted]

Stipulation Annexed to Order

It is hereby stipulated and agreed by and between the solicitors for the respective parties hereto that the time for the defendants-appellants, Maxime H. Furlaud and Kingston Corporation to serve and file the record on appeal in the office of the Clerk of the United States Circuit Court of Appeals for the Second Circuit, be and the same hereby is extended up to and including the 6th day of October, 1933.

Dated New York, September 20, 1933.

Eppstein & Hirshfield, Solicitors for Defendants-Appellants, Kingston Corporation and Maxime H. Furlaud. Ehrich, Royall, Wheeler & Walter, Solicitors for Complainant-Appellee.

[fol. 368] In United States District Court, Southern District of New York

[Title omitted]

Order Extending Term Until October 6, 1933 (George W. McCandless)

Upon the annexed stipulation, it is, now, on motion of Ehrich, Royall, Wheeler & Walter, solicitors for the complainant-appellee-appellant, George W. McCandless, as Receiver of Duquesne Gas Corporation,

Ordered, that the time for the complainant-appellee-appellant to serve and file his record on appeal in the above matter in the office of the Clerk of the United States Circuit Court of Appeals, for the Second Circuit, be and the same hereby is extended up to and including the 6th day of October, 1933.

Dated New York City, September 25th, 1933.

Charles Weiser, Clerk of the United States District Court, Southern District of New York.

[fol. 369] IN UNITED STATES DISTRICT COURT

[Title omitted]

STIPULATION ANNEXED TO ORDER

It is hereby stipulated and agreed by and between the solicitors for the respective parties hereto that the time for the complainant-appellant George W. McCandless to serve and file the record on cross appeal in the office of the Clerk of the United States Circuit Court of Appeals for the Second Circuit, be and the same hereby is extended up to and including the 6th day of October, 1933, and that an order may be entered hereon without further notice.

Dated, New York, September 20, 1933.

Ehrich, Royall, Wheeler & Walter, Solicitors for Complainant-Appellant; Eppstein & Hirshfield, Solicitors for Defendants-Appellees.

[fol. 370] IN UNITED STATES DISTRICT COURT, SOUTHERN DISTRICT OF NEW YORK

[Title omitted]

STIPULATION AS TO RECORD

It is hereby stipulated and agreed by and between the attorneys for the respective parties hereto that the foregoing is a complete statement of the record in the District Court as agreed on by the parties, and that the same be filed in lieu of the original papers herein.

Dated, New York, October 3rd, 1933.

Eppstein & Hirshfield, Attorneys for Appellants Maxime H. Furlaud and Kingston Corporation and Byron Corporation and Chaucer Corporation, Appellees; Ehrich, Royall, Wheeler & Walter, Attorneys for Complainant-Appellee-Appellant.

[fol. 371] In United States District Court, Southern District of New York

[Title omitted]

Order Filing Record

Upon the foregoing consent of the attorneys for the respective parties, the printed record is hereby ordered filed in lieu of the original papers for the purpose of certifying the record on appeal.

Dated, October —, 1933.

John C. Knox, U. S. D. J.

[fol. 372] Clerk's certificate to foregoing transcript omitted in printing.

[fol. 373] UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT, OCTOBER TERM, 1933

Argued December 11, 1933. Decided January 8, 1934

No. 199

GEORGE W. MCCANDLESS, as Receiver, etc., Plaintiff-Appel-CORPORATION, Complainant-Appellee-Appellant

v.

MAXIME H. FURLUND and KINGSTON CORPORATION, Defendants-Appellants-Appellees, and Byron Corporation and Chaucer Corporation, Defendants-Appellees, and Carlos Reuter, Defendant

Appeal from the District Court of the United States for the Southern District of New York

Before Manton, L. Hand, and Chase, Circuit Judges

Suit by George W. McCandless, receiver of Duquesne Gas Corporation, to recover for breach of trust and resulting damages. Decree for the plaintiff against the defendants Maxime H. Furlaud and the Kingston Corporation, and dismissing the bill against the Byron Corporation and Chaucer Corporation. Defendants Furlaud and Kingston Corporation appeal; plaintiff also appeals. Decree reversed, with directions to dismiss the bill.

Ehrich, Royall, Wheeler & Walter, of New York City (Ralph Royall, Bartow H. Hall, and James G. Holland, all of New York City, and William A. Magee, and Clark Miller, both of Pittsburgh, Pa., of counsel), for complainant.

Eppstein & Hirschfield, of New York City (Louis B. Eppstein, Ira W. Hirshfield, and Louis J. Altkrug, all of New York City, of counsel), for appellants Maxime H. Furland and Kingston Corporation.

MANTON, Circuit Judge.

These are cross-appeals. Furlaud and Kingston Corporation appeal from a judgment of $1,834,640.08 against them for damages for breach of trust. The receiver ap-

peals from a refusal to decree $850,000 more; also from the dismissal of the suit against the Byron Corporation and Chaucer Corporation.

The plaintiff was appointed receiver of the Duquesne Gas Corporation in the Western District of Pennsylvania, having been appointed such on a stockholder's bill and a consent thereto by the Duquesne Gas Corporation. The bill of complaint, in this suit, alleges the appointment in the Western District of Pennsylvania, on January 19, 1932, stating that the receiver was appointed "of all the assets and property, including choses in action, of said Duquesne Gas Corporation, and the complainant has duly qualified and is now acting as such Receiver; that upon petition of the complainant as such Receiver duly filed in the United States District Court, in and for the Southern District of New York, an order was duly made on the 23rd of March, 1932 by said last mentioned Court appointing said complainant George W. McCandless, as Ancillary Receiver of Duquesne Gas Corporation which last men- [fol. 374] tioned order duly authorized the complainant, as such Receiver, to bring this suit, and the complainant has duly qualified and is now acting as such Ancillary Receiver."

The answer of the defendants denied this allegation and required proof thereof. The order appointing the plaintiff ancillary receiver after reciting the appointment in the Western District of Pennsylvania reads:

"Ordered, adjudged and decreed that George W. McCandless be and he is hereby appointed ancillary receiver of Duquesne Gas Corporation in and for the Southern District of New York to carry into force and effect the order of the court of original jurisdiction, and it is further

"Ordered, adjudged and decreed that said ancillary receiver is hereby authorized to bring an action against the promoters of said corporation * * * for an accounting and for the restitution of funds * * *."

The substance of this bill is that the banking house of Furlaud & Co., Inc., of which the defendant Furlaud was president, received the proceeds of a public sale of securities of the Duquesne Gas Corporation in a fiduciary capacity, for that corporation, and became accountable as a

trustee but, instead of accounting for the fund, diverted and misappropriated about one-half of the moneys received; that they caused the corporation Furlaud & Co., Inc., to be dissolved; that the defendants Kingston Corporation, Byron Corporation, and Chaucer Corporation were dummy corporations, used in attempting to cover up diversions and misappropriations.

This claim arises out of the following facts: Furlaud & Co., Inc., of New York City with offices there, early in 1930, with the defendant Furlaud, carried on a banking business. He and one Reuter, not served with process, were the chief stockholders and with other employees, directors, and officers, early in 1930, negotiated with the owners of nine gas properties located in the Pittsburgh, Pa., region and obtained options, without consideration, for their purchase by the Kingston Corporation. They employed an engineering firm, and about February 1, 1930, it made written reports appraising five of the properties at $1,700,000. These were purchased at about $1,300,000. The other four properties were appraised by other engineers at $5,000,000 in February, 1930, and the purchase price was about $1,200,000. Thereupon the Duquesne Gas Corporation was organized in Pennsylvania with 1,000 shares of no par value. In February, 1930, it was arranged with the various optionors for the execution of the assignments of the various gas properties by placing instruments of conveyance in escrow with banks located in Pittsburgh and Washington, Pa., and other convenient places. The instruments of conveyance, as deposited, ran to the gas corporation as transferee. The deposit agreement provided that the escrow banks, when notified by Furlaud, were to present drafts upon the Duquesne Gas Corporation for the respective balances of the purchase price, payable in New York, and that the banks, upon having telegraphic advices from their correspondent banks in New York that the drafts had been accepted, were to deliver the conveyances to named persons being the employees of the firm of attorneys who were in charge of carrying out the corporate proceedings. The aggregate balance of the purchase price of the nine properties payable under the escrow agreements was $2,449,900.

There was organized a bankers' syndicate and a distributing group for the issuance and sale of $4,000,000 of Duquesne Gas Corporation first mortgage 6 per cent con-

veritble gold bonds. Furland & Co., Inc., were the syndicate managers and, with four other banking houses, publicly announced the issue for sale on March 25, 1930, and about forty dealers in securities became the distributing group and sold the bonds. They were offered at 97½ and the distributing group were given 4 per cent. commission. Necessary proceedings were taken for the authorization of the bond issue, with a corporate mortgage to secure it, and for an issue of $1,000,000 of notes and for an increase of the capital stock from 1,000 shares to 1,250,000 shares without par value. The security for the bond issue was a mortgage covering the properties. It was out of these funds that payments for the oil properties were made. In our disposition of the case, it is sufficient to say that the net proceeds from the sale of the $4,000,000 bond issue is shown to have been $3,631,671.04; from the sale of the total note issue, $861,097.69; from the sale of 85,000 shares of stock, $850,000—a total of $5,342,768.23. The cost of the properties, including the working capital put in by the bankers, amounted to $2,937,989. It is shown that the amount received by the bankers from the bonds, notes, and [fol. 375] stocks now claimed to have been diverted and misappropriated to their own use, is $2,404,779.73. Whether this was a misappropriation of the funds or a legitimate profit we need not now decide.

The legal sufficiency of the appointment of the plaintiff as an ancillary receiver in the Southern District of New York was put in issue by the answer and he bears the burden of establishing its legality. Grant v. Leach & Co., 280 U. S. 351, 50 S. Ct. 107, 74 L. Ed. 470. The record of the ancillary proceedings in evidence consisted of: (a) A petition of the receiver, captioned "Frank T. Harrington, Complainant, against Duquesne Gas Corporation, Defendant," in the United States District Court for the Southern District of New York and annexed to the petition; (b) the amended bill of complaint filed in the Western District of Pennsylvania, captioned "Frank T. Harrington, Complainant, against Duquesne Gas Corp., Defendant"; (c) amendment to the prayer for relief in the action in the Western District of Pennsylvania; (d) answer of the defendant in the action referred to in (b); (e) a certified copy of the resolution of the board of directors of the Duquesne Gas Corporation, annexed to the answer filed in the Western

District of Pennsylvania; (f) the answer of the defendant Duquesne Gas Corporation filed in Pennsylvania action brought in the Western District by the trustee under the first mortgage of the Duquesne Gas Corporation; (g) the decree entered in the Western District of Pennsylvania; (h) a certificate of the clerk of the District Court for the Western District of Pennsylvania, certifying that a receiver's bond of $50,000 had been filed. On these papers the District Court for the Southern District of New York appointed the plaintiff ancillary receiver of the Duquesne Gas Corporation in this district, and authorized the suit to be brought against the promoters of the corporation for an accounting and for the restitution of funds, fraudulently diverted and misappropriated, and for secret and excessive profits. Thus, upon the petition alone of a foreign federal receiver, an ancillary receiver is appointed, where no bill had been filed in the jurisdiction by any party aggrieved praying for such relief. No process was issued in this jurisdiction and there has been no appearance or answer filed by the corporation within the district. This suit was instituted shortly after such appointment.

It has long been settled that an equity receiver is an officer of the court appointing him and, as such, he has no status and cannot be sued in a district other than the one in which he was appointed and he cannot recover property or assets of the corporation in receivership even though he may have been authorized to do so by the court of his original appointment. Booth v. Clark, 17 How. 322, 15 L. Ed. 164; Sterett v. Second Natl. Bank, 248 U. S. 73, 39 S. Ct. 27, 63 L. Ed. 135; Great Western Mining & Mfg. Co. v. Harris, 198 U. S. 561, 25 S. Ct. 770, 49 L. Ed. 1163; Hale v. Allinson, 188 U. S. 56, 23 S. Ct. 244, 47 L. Ed. 380. Nor may foreign receivers sue outside the district as a matter of comity even by obtaining permission before suit is commenced. Moore v. Mitchell, 281 U. S. 18, 24, 50 S. Ct. 175, 74 L. Ed. 673; Fowler v. Osgood, 141 F. 20, 4 L. R. A. (N. S.) 824 (C. C. A. 8). Moreover, the usual practice is to obtain an ancillary receiver by an independent bill requesting it. Indeed, it has been said that such an independent bill is required. Mercantile Trust Co. v. Kanawha Ry. Co. (C. C.) 39 F. 337. Even if there are assets in the foreign jurisdiction, the court there has a right to appoint a receiver only in a pending suit where independent relief

is asked. To permit a foreign receiver to obtain an ancillary appointment, on an ex parte application, improperly avoids the rule denying foreign receivers the right to sue in the foreign jurisdiction. The appointment of such receivers does not give him authority to acquire possession of property beyond the jurisdiction of his appointment. The right of a receiver to sue in a foreign court cannot be upheld as a mere incident to the office of a receiver. The appointing court cannot clothe him with such power and any attempt to confer any such authority on him is futile. Hilliker v. Hale (C. C. A.) 117 F. 220; Greene v. Star Cash & Package Co. (C. C.) 99 F. 656; In re Brant (C. C.) 96 F. 257; Mercantile Trust Co. v. Kanawha Ry C. (C. C.) 39 F. 337. The authority to sue is sufficiently raised by the denial of the allegation that the receiver was duly appointed. Grant v. Leach & Co., 280 U. S. 351, 50 S. Ct. 107, 74 L. Ed. 470; Fairview, etc., Co. v. Ulrich, 192 F. 894 (C. C. A. 7).

While ancillary receiverships are usually conducted in the spirit of comity, with a view of avoiding unnecessary conflict in the administration of the trust, they are, however, [fol. 376] in all respects the proceedings in two respective causes, each resting upon its own distinct basis. Ancillary proceedings are independent suits and there must be a plaintiff and a defendant and the first must be one who claims injury committed by the defendant. One who is not aggrieved cannot come into court and ask for the appointment of an ancillary receiver. Lack of title to the property is more than a mere technicality. It involves the very substance of a right to file the independent bill, Street's Equity Practice, vol. 3, § 2542; Walker v. U. S. Light & Heating Co. (D. C.) 220 F. 393. The appointment of the plaintiff as ancillary receiver was void, and he did not acquire, in any of the proceedings, a status to warrant the institution of this suit.

Decree reversed.

[fol. 377] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a Stated Term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the Court Rooms in the Post Office Building in the City of New York,

on the 15th day of January, one thousand nine hundred and thirty-four.

Present: Hon. Martin T. Manton, Hon. Learned Hand, Hon. Harrie B. Chase, Circuit Judges.

GEORGE W. MCCANDLESS, as Receiver, Etc., Plaintiff-Appellant,

vs.

MAXIME H. FURLUND and KINGSTON CORPORATION, Defendants-Appellants; Byron Corporation and Chaucer Corporation, Defendants-Appellees; Carlos Reuter, Defendant

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the decree of said District Court be and it hereby is reversed with costs to the defendants.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

Wm. Parkin, Clerk.

[fol. 378] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. George W. McCandless, as Receiver, Etc., vs. Maxime H. Furlaud, et al. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Jan. 15, 1934. William Parkin, Clerk.

[fol. 379] UNITED STATES OF AMERICA, ss:

The President of the United States of America, to the Honorable the Judges of the United States Circuit Court of Appeals for the Second Circuit; Greeting:

Greeting:

Whereas, lately in the United States Circuit Court of Appeals for the Second Circuit, in a cause between George W. McCandless, as Receiver of Duquesne Gas Corporation, Complainant-Appellee-appellant, and Maxime H. Furlaud and Kingston Corporation, Defendants-Appellants-Appel-

lees, and Byron Corporation and Chaucer Corporation, Defendants-Appellees, et al., No. 199, wherein the decree of the said Circuit Court of Appeals, entered in said cause on the 15th day of January, A. D. 1934, is in the following words, viz;

"This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the decree of said District Court be, and it hereby is reversed with costs to the defendants.

It is further ordered that a mandate issue to the said District Court in accordance with this decree."

as by the inspection of the transcript of record of the said United States Circuit Court of Appeals which was brought into the Supreme Court of the United States by virtue of a writ of certiorari granted upon the petition of George W. McCandless, as Receiver, but limited to the questions pertaining to the validity of the appointment of the petitioner as ancillary receiver, and his right as such to maintain this suit, agreeably to the Act of Congress, in such case made and provided, fully and at large appears

And whereas, in the present term of October, in the year of our Lord, one thousand nine hundred and thirty-four, the said cause came on to be heard before the said Supreme Court, on the said transcript of record, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the decree of the said United States Circuit Court of Appeals in this cause be, and the same is hereby, reversed with costs; and that George W. McCandless, as Receiver, etc., recover against Maxime H. Furlaud, et al., Three Hundred and One Dollars and Five Cents for his costs herein expended and have execution therefor.

[fol. 380] And it is further ordered, That this cause be, and the same is hereby, remanded to the said Circuit Court of Appeals for further proceedings in conformity with the opinion of this Court and for the determination of the questions relating to the liability of the defendants decided by the District Court and presented by the appeal and cross appeal.

November 5, 1934.

You, therefore, are hereby commanded that such execution and further proceedings be had in such cause, in conformity with the opinion and decree of this Court, as according to right and justice, and the laws of the United States, ought to be had, the said writ of certiorari notwithstanding.

Witness, the Honorable Charles E. Hughes, Chief Justice of the United States, the eleventh day of December, in the year of our Lord one thousand nine hundred and thirty-four.

Costs of McCandless, as Receiver.

Clerk	$136.05
Printing record	145.00
Attorney	20.00
	$301.05

Charles Elmore Cropley, Clerk of the Supreme Court of the United States.

[fol. 381] SUPREME COURT OF THE UNITED STATES—OCTOBER TERM, 1934

Costs of George W. McCandless, as Receiver of Duquesne Gas Corporation

—— in No. 11

1933, October Term—Docketing cause and filing record, $10.00; appearance .25; filing precipe .25; filing papers $3.00; filing briefs $5.00; submission, .20; Order .20; filing and recording .65; certified copy of the order, $2.50; continuance, .25.

193-, October Term—Transfer, $1.00; filing and receipt, .25; filing papers, $4.25; filing briefs $5.00; argument, .20; decree $1.00; filing same, .25; recording, .40; mandate, $5.00; preparing record for printer, etc., $96.00; cost of printing record, $145.00; attorney's docket fee, $20.00; costs and copy, .40; 301.05

301.05

Fee Book, page 38504.

Test:

Charles Elmore Cropley, Clerk of the Supreme Court of the United States. H. W. Barr.

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United States Circuit Court of Appeals

FOR THE SECOND CIRCUIT.

GEORGE W. MCCANDLESS, as Receiver of Duquesne Gas Corporation,
Complainant-Appellee-Appellant,

against

MAXIME H. FURLAUD and KINGSTON CORPORATION,
Defendants-Appellants-Appellees,

and

BYRON CORPORATION and CHAUCER CORPORATION,
Defendants-Appellees,

and

CARLOS REUTER,
Defendant.

Before: MANTON, L. HAND and CHASE,
Circuit Judges.

Appeal from the United States District Court for the Southern District of New York. Decree for plaintiff awarding damages on an accounting against the defendants Maxime H. Furlaud and

Kingston Corporation only, who appeal. Decree reversed.

EHRICH, ROYALL, WHEELER & WALTER, Esqs.,
Solicitors for Plaintiff.
Ralph Royall, Esq.
James G. Holland, Esq.
William A. Magee, Esq.
Of Counsel.

EPPSTEIN & HIRSHFIELD, Esqs.,
Solicitors for Defendants, Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation.
Louis B. Eppstein, Esq.
Ira W. Hirshfield, Esq.
Louis J. Altkrug, Esq.
Of Counsel.

MANTON, *Circuit Judge.*

The defendants, Maxime H. Furland and Kingston Corporation, appeal from a decree awarding the plaintiff the sum of $1,834,640.08 in the accounting suit for all funds or moneys coming into the hands of the defendants or any of them from the sale of bonds, notes and shares of stock of the Duquesne Gas Corporation.

A receiver was appointed for the Duquesne Gas Corporation in the United States District Court for the Western District of Pennsylvania, and he sued in the District Court for the Southern District of New York, without appointment therein as an ancillary receiver. We reversed the decree, on a former appeal, for failure to have an ancillary

receiver appointed in the Southern District of New York before suit (68 Fed. 2, 925). The Supreme Court reversed (79 Law. Ed. 32) remanding the cause to this court to pass upon the merits of the issues presented.

The gravamen of the bill of complaint is to be found in para. 17, which alleges that the receiver is entitled, on behalf of the Duquesne Gas Corporation, to have the defendants' account to the corporation "for the funds or moneys coming into their hands or into the hands of any of them or their agents or representatives from the sale of the securities of said Duquesne Gas Corporation or of any of said securities, and for the disposition made of such funds or moneys and to make restitution for any or all of such funds or moneys wrongfully diverted from Duquesne Gas Corporation and misappropriated or converted by the defendants or any of them to their own uses and for any or all secret or excessive profits taken or retained by them * * *."

The prayer for relief asked that the defendants be compelled to account, "for all funds or moneys coming into the hands of them or any of them or of the agents or representatives of any of them or in the hands of any one else acting with or for them from the sale of the bonds, notes and shares of stock of said Duquesne Gas Corporation."

The Kingston Corporation was organized under the New Jersey laws March 10, 1926; Furland & Company Inc. incorporated under the New York laws July 18, 1928. The latter was authorized to promote and assist in the financing of corporations, firms and syndicates in selling issues of securities. Defendant Maxime H. Furland was its president.

In 1929, the Kingston Corporation, a wholly owned subsidiary of Furland & Company Inc., ob-

tained options on various oil and gas properties in Western Pennsylvania, at a total purchase price of $2,572,989. Some of these options were taken in the name of an individual and later assigned to the Kingston Corporation. The properties were examined by engineers and appraisals were made; some, examined by one firm, at $4,929,787, and others, by another engineer, at $1,743,520. On February 21, 1930, Furlaud & Company Inc. caused the Duquesne Gas Corporation to be organized under the Pennsylvania laws with a capital issue of 1,000 shares of no-par value common stock. This was all subscribed and paid for by Furlaud & Company, Inc. at 50¢ a share, a price authorized by the Board of Directors of the Duquesne Gas Corporation. Arrangements were then made for the owners of the optional properties to execute deeds to the Duquesne Gas Corporation to be held in escrow in various banks in and around Western Pennsylvania, with directions to deliver them upon the payment of the purchase price. Prior to the date of closing, April 9, 1930, a bankers syndicate was organized consisting of Furlaud & Company Inc. as managers and other banking houses, to purchase, when and if issued and to distribute in allotted territories, first mortgage 6% gold bonds of the Duquesne Gas Corporation of a par value of $4,000,000 which it was arranged the Duquesne Gas Corporation would issue. On March 19, 1930, Furlaud & Company, Inc., as such distributing group manager, advised security dealers by letter that it had purchased "when, as and if issued" the bonds of the Duquesne Gas Corporation, and offered to sell these securities to the dealers for resale by them. A subscription blank accompanied the offer. It was filled in and returned to Furlaud & Company Inc. with each dealer's order. On March 25,

1930, an advertisement appeared in a New York newspaper over the names of the five members of the bank syndicate, offering the securities for sale. At this time, when the entire stock of the Duquesne Gas Corporation was held by Furland & Company Inc., the gas company authorized the issuance of four million dollars first mortgage bonds, and also one million dollars, 6½% notes to be secured by mortgages, and the authorized capital stock was increased from 1,000 to 1,250,000 shares of common stock without par value.

On April 7, 1930, an agreement of reorganization was entered into between the Duquesne Gas Corporation and the Kingston Corporation by which the latter agreed it would cause the optioned properties, all its assets other than cash, to be transferred to the Duquesne Gas Corporation, which in turn agreed to issue to the Kingston Corporation 535,000 shares of common stock without par value and $1,300,000 principal amount of convertible gold bonds and to issue an obligation of the Kingston Corporation to the Central Hanover Bank & Trust Company in the sum of $3,015,000. Prior to the closing on April 9, 1930, two loans were made by the Central Hanover Bank & Trust Company, one for $3,015,000 for the Kingston Corporation and the other for $3,379,500 to Furland & Company, Inc.

The Kingston Corporation, at the closing, delivered its certified checks, drawn on the Central Hanover Bank & Trust Company for a total of $2,449,900 to the Equitable Trust Company, the Guarantee Trust Company of New York, and the Central Hanover Bank & Trust Company respectively. These checks put the banks in funds to meet the drafts, in their hands, drawn on the Kingston Corporation by the banks in Western Pennsylvania,

which held in escrow the deeds transferring the properties to the Duquesne Gas Corporation. The Western Pennsylvania banks released the deeds upon being notified of the aforesaid payments. Upon receiving telegraphic and telephonic advice that the deeds had been recorded, the Duquesne Gas Corporation issued the securities to the Kingston Corporation in accordance with the terms of the reorganization agreement. At the same time Furlaud & Company Inc., pursuant to an agreement of April 7, 1930, delivered its check, drawn on the Central Hanover Bank & Trust Company, for $3,379,500 to the Duquesne Gas Corporation as the purchase price for $2,700,000 par value 6% bonds at 90, and $1,000,000. 6½% gold notes of the Duquesne Gas Corporation at 88; and 139,000 shares of its common stock at 50c a share. These securities were immediately delivered to Furlaud & Company Inc. Duquesne Gas Corporation then drew its check for $3,015,000 to the order of the Central Hanover Bank & Trust Company in payment of the Kingston Corporation's one-day loan, the payment of which the Duquesne Gas Corporation had assumed. The Duquesne Gas Corporation then had left in its treasury $365,000.

On the day of the closing, some of the security dealers, who had agreed to purchase about $2,350,000 face value of the bonds, sent their representatives to the Central Hanover Bank & Trust Company with checks payable to the order of Furlaud & Company, Inc., and picked up the bonds which they had agreed to purchase. The checks thus received totaled $1,886,330. Furlaud & Company Inc. then paid its loan to the Central Hanover Bank & Trust Company by the application of $1,886,330; $700,000 it had borrowed from the Chatham & Phenix National Bank & Trust Co.; $300,000 bor-

rowed from the Hibernia Trust Company, and $500,000 borrowed from the Pacific Trust Company. Furlaud & Company Inc. then paid its other bank loans. The Kingston Corporation turned over to Furlaud & Company Inc. $300,000, certain expense moneys advanced by Furlaud & Company Inc. in connection with the acquisition of the properties, and at the same time the Kingston Corporation loaned Furlaud & Company Inc. $265,000. The entire issue of bonds was not disposed of on April 9, 1930, and Furlaud & Company Inc. organized a secondary distributing group in August, 1930, to sell them. Furlaud & Company Inc. made purchases in the open market totaling $1,194,000. which it disposed of from time to time up to July, 1931. A few weeks after the closing, Furlaud & Company Inc. sold the one million dollar gold note issue to another security house for $886,546.56. Maxime H. Furlaud had no relation to these transactions other than as an officer and director of Furlaud & Company Inc., and his personal activity in carrying on the negotiations and transactions. He did not participate in the alleged fraudulent appraisal or receive personally any of the moneys paid to Furlaud & Company Inc.

The recovery below seems to be grounded upon the supposed right of a receiver in sequestration proceedings to recover profits made, which the court thought excessive, and in legal effect, to say that all the moneys resulting from the sale of the securities were held in trust for the benefit of the Duquesne Gas Corporation. Furlaud is held individually on the theory of a breach of trust. No trust funds ever came into his hands.

As stated by the court below:

> "At the time that the transactions through which Duquesne Gas Corporation acquired the

> various gas properties were consummated, and for some time thereafter, Furlaud & Company Inc., owned every share of its capital stock, and ratified and approved of the whole transaction."

At the end of these transactions, the two corporations, Furlaud & Company Inc. and its subsidiary, Kingston Corporation, owned all of the issued common capital stock of the Duquesne Gas Corporation, and all of its bonds and notes. No other person purchased from Duquesne Gas Corporation a share of stock, a bond or a note. Neither a corporation nor its receiver has any right of action against the organizers of the corporation for the recovery of profits made by such organizers in the sale of securities, where the organizers became the owners of all the authorized and outstanding stock of the corporation. *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206; *Ball* v. *Breed*, 294 Fed. 227.

The receiver now contends that misrepresentations as to the value of the properties transferred were made on their resale to the Duquesne Gas Corporation. If such be the fact, the receiver may not recover therefor. *Old Dominion Copper Co.* v. *Lewisohn, supra.* As there stated:

> "If there was a wrong, it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation *nunc pro tunc*, but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. For it is only by virtue of the innocent

> subscribers' position and the promoter's invitation that the corporation has any pretense for a standing in court. If the promoters, after starting their scheme, had sold their stock before any subscriptions were taken, and then the purchasers of their stock, without notice, had invited the public to come in, and it did, we do not see how the company could maintain this suit. If it could not then, we do not see how it can now."

The principle announced in *Ball* v. *Breed, supra,* by this court, is applicable here. There a suit was brought by a receiver on the theory that the profits made by the promoters were without the knowledge and consent of the corporation, and that the corporation does not consent if any existing stockholder is ignorant of a transaction involving a so-called secret profit. There the secret profit was a matter of contract between one who had acquired an option to purchase the stock, securities and indebtedness of a corporation, and bankers. The bankers owned all the preferred, common and founders' stock subscribed for or intended to be issued. No other persons had rights to receive stock from the corporation. There were no innocent stockholders. This court said:

> "If, then, there was a fraud, it was not against the corporation, and a cause of action, if any, is personal to the purchasers of the stock. The fraud, if any, is what has been called a subsidiary fraud not affecting the corporation."

In the instant case, as in the *Ball* case, at the conclusion of the transaction between the organizers of the corporation and the corporation, all of the

stocks and securities authorized and issued and intended to be issued by the corporation belonged to the persons of whose actions the receiver now complains. In the instant case, the organizers of the corporation, in addition to receiving stock of the Duquesne Gas Corporation, also received its bonds and notes, thus embracing all the securities issued. These circumstances forbid the plaintiff maintaining that a trust was created for any alleged unreasonable profit or any other sums that should have been placed in the treasury of the corporation as a result of the sale of the securities. *Blum* v. *Whitney*, 185 N. Y. 232; *Seymour* v. *Spring Forest Cemetery Asso.*, 144 N. Y. 333; *Wells* v. *Northern Trust Co.*, 195 Ill., 288; *Allenhurst Park Estates* v. *Smith*, 101 N. J. Equity, 581; *Tompkins* v. *Sperry, Jones & Co.*, 96 Med. 560; *Hayes* v. *The Georgian*, 280 Mass. 10.

But the court below said the bondholders were induced to purchase the securities so issued by the Duquesne Gas Corporation by misrepresentations, and, as a result, a trust in favor of the corporation arose. Citing, *McKee* v. *Mamon*, 159 U. S. 317; *Sayer* v. *Wynkoop*, 248 N. Y. 54. In the *McKee* case, the money was turned over to McKee in trust requiring him "to pay over to all parties who have rendered services in the prosecution of this claim the amount due to such persons". In the *Sayer* case, the money was due to an insurance company as premiums on policies and the debtor made payment to his broker with instructions to pay these premiums. In each case a property right existed in favor of the plaintiff in the fund delivered to the trustee for a specific purpose. Here, if any misrepresentation was made in the sale of the securities under the circumstances above described, a cause of action might exist against Furland & Com-

pany, Inc. or the other banking houses, by the security holders, but no trust was created in favor of the corporation for any of the moneys received. *Piggly-Wiggly Delaware, Inc.* v. *Bartlett,* 95 N. J. Equity, 469; *Whitten* v. *Dabney,* 171 Cal. 621; *Turner* v. *Markham,* 155 Cal. 562; *Vigers* v. *Pike,* 8 Cl. & F. 562.

To be sure, in so far as the property of the corporation is concerned, the receiver holds it for the benefit of all creditors. As to such property, he may be regarded as a trustee. The property that is transferred to him as the receiver of such corporation for administration is the property of the corporation. This does not include any personal rights or property belonging to others who are not parties to the receivership proceedings. It does not include the personal rights of the individuals who have become bondholders. To establish a cause of action, for the bondholders, for fraud in the issuance of these bonds, it is necessary to allege and prove not only that false representations were made, but that they were materially so. It is also essential to show that the purchaser relied upon such misrepresentations and believed them to be true, acting upon them and making his investments upon such reliance. *Scovil* v. *Thayer,* 105 U. S. 143; *Foster* v. *Seymour,* 23 Fed. 65. And if there be any wrong, it was a wrong individual to the bondholders; it was not a wrong against the Duquesne Gas Corporation, at least such as can be held to be the result of a breach of trust as pleaded and claimed in support of this cause of action. Cross bill affirmed with directions to dismiss the bill.

Decree reversed.

[fol. 393] UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

At a stated term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the court-rooms in the Post Office building, in the City of New York, on the 11th day of March, one thousand nine hundred and thirty-five.

Present: Hon. Martin T. Manton, Hon. Learned Hand, Hon. Harrie B. Chase, Circuit Judges.

GEORGE W. MCCANDLESS, as Receiver, etc., Plaintiff-Appellant,

vs.

MAXIME H. FURLAUD and KINGSTON CORPORATION, Defendants-Appellants

Appeal from the District Court of the United States for the Southern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the decree of said District Court be and it hereby is reversed, and affirmed as to the cross appeal with directions to dismiss the bill. Costs of the appeal to the defendants.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

WM. PARKIN, Clerk.

[fol. 394] [Endorsed:] United States Circuit Court of Appeals, Second Circuit. George W. McCandless, as Receiver, etc., vs. Maxime H. Furlaud et al. Order for Mandate. United States Circuit Court of Appeals, Second Circuit. Filed Mar. 11, 1935. William Parkin, Clerk.

[fol. 395] UNITED STATES OF AMERICA, SOUTHERN DISTRICT OF NEW YORK

I, William Parkin, Clerk of the United States Circuit Court of Appeals for the Second Circuit, do hereby certify

that the foregoing pages, numbered from 1 to 394, inclusive, contain a true and complete transcript of the record and proceedings had in said Court, in the case of George W. McCandless, as Receiver, etc., Plaintiff-Appellant, against Maxime H. Furlund and Kingston Corporation, Defendant-Appellant, as the same remain of record and on file in my office.

In testimony whereof, I have caused the seal of the said Court to be hereunto affixed, at the City of New York, in the Southern District of New York, in the Second Circuit, this 16th day of April, in the year of our Lord one thousand nine hundred and thirty-five, and of the Independence of the said United States the one hundred and fifty-ninth.

Wm. Parkin, Clerk. (Seal United States Circuit Court of Appeals for the Second Circuit.)

[fol. 396] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed May 13, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 39,508. U. S. Circuit Court of Appeals, Second Circuit, Term No. 26. George W. McCandless, as Receiver of Duquesne Gas Corporation, Petitioner, vs. Maxinme H. Furlaud, Kingston Corporation, Byron Corporation, et al. Petition for a writ of certiorari and exhibit thereto. Filed April 18, 1935. File No. 26 O. T. 1935.

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APR 1
CHARLES EL

IN THE

Supreme Court of the United States

OCTOBER TERM, 1934

No. 826

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,
Petitioner (Plaintiff-Appellee-Appellant Below),
against
MAXIME H. FURLAUD and KINGSTON CORPORATION,
Defendants-Appellants-Appellees Below,
and
BYRON CORPORATION and CHAUCER CORPORATION,
Defendants-Appellees Below,
and
CARLOS REUTER,
Defendant Below.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF

RALPH ROYALL,
WILLIAM A. MAGEE and
CLARK MILLER,
Counsel for Petitioner.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934

No.

GEORGE W. MCCANDLESS, as Receiver of Duquesne Gas Corporation,
Petitioner (Plaintiff-Appellee-Appellant Below),
against
MAXIME H. FURLAUD and KINGSTON CORPORATION,
Defendants-Appellants-Appellees Below,
and
BYRON CORPORATION and CHAUCER CORPORATION,
Defendants-Appellees Below,
and
CARLOS REUTER,
Defendant Below.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable Charles E. Hughes, the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

George W. McCandless, as Receiver of Duquesne Gas Corporation, plaintiff-appellee-appellant below, the above

named petitioner, respectfully prays that a writ of certiorari issue to review the decree of the United States Circuit Court of Appeals for the Second Circuit, filed on the 11th day of March, 1935, reversing the final decree filed in the United States District Court for the Southern District of New York on the 11th day of May, 1933, which awarded a judgment to plaintiff against the defendants Maxime H. Furlaud and Kingston Corporation in the sum of $1,834,640.08.

STATEMENT

This is a suit brought by the petitioner as plaintiff in his capacity as ancillary receiver of Duquesne Gas Corporation, appointed as such in the District Court of the United States for the Southern District of New York (R. 5-7). After a trial before United States District Judge Knox, a decree was made awarding judgment to the plaintiff against the defendants Maxime H. Furlaud and Kingston Corporation in the sum of $1,834,640.08 and dismissing the complaint as to the defendants Byron Corporation and Chaucer Corporation (R. 339-40). The defendant Carlos Reuter was not served with process and did not appear (R. 1).

The defendants Maxime H. Furlaud and Kingston Corporation appealed from such decree to the Circuit Court of Appeals, Second Circuit, and the plaintiff took a cross appeal claiming that judgment should be awarded against each of the defendants Byron Corporation and Chaucer Corporation in the sum of $425,000 with interest, and also that the judgment against the defendants Maxime H. Furlaud and Kingston Corporation should be increased by the amount of $850,000 with interest.

Upon the appeal the defendants Maxime H. Furlaud and Kingston Corporation raised for the first time the question of the plaintiff's right to sue. The claim of these defendants was that the appointment of the plaintiff as ancillary receiver in the District Court for the Southern District of New York was void and that such appointment could be collaterally attacked and that the judgment which had been granted in favor of the plaintiff as such ancillary receiver should be vacated and set aside. The Circuit Court of Appeals adopted this view and by a decree dated the 8th day of January, 1934, reversed the judgment.

On the petition of the plaintiff, the Supreme Court granted a writ of certiorari to review the decree of the Circuit Court of Appeals dated the 8th day of January 1934, and limited such writ to the review of the questions relating to the validity of the appointment of the ancillary receiver (292 U. S. 617; 78 L. Ed. 1475). Upon the appeal, pursuant to the writ, the Supreme Court reversed the Circuit Court of Appeals and held that the validity of the appointment of the plaintiff as ancillary receiver could not be first questioned on appeal and directed a rehearing of the appeal in the Circuit Court of Appeals for the determination of the questions relating to the liability of the defendants decided by the District Court* (79 L. Ed. 32).

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*The opinion of the Circuit Court of Appeals upon the rehearing erroneously states in the second paragraph thereof:

> "A receiver was appointed for the Duquesne Gas Corporation in the United States District Court for the Western District of Pennsylvania, and he sued in the District Court for the Southern District of New York, without appointment therein as an ancillary receiver. We reversed the decree, on a former appeal, for failure to have an ancillary receiver appointed in the Southern District of New York before suit (68 Fed. 2, 925). The Supreme Court reversed (79 Law. Ed. 32) remanding the cause to this court to pass upon the merits of the issues presented."

Upon a rehearing pursuant to the Supreme Court's mandate, the Circuit Court of Appeals reversed the judgment of the District Court on the merits. The opinion upon such reversal by Manton, *J.* is not yet reported.

The plaintiff now seeks by this petition a writ of certiorari to review the decree of reversal of the United States Circuit Court of Appeals, dated the 11th day of March 1935.

The subject matter of the suit is the promoting in 1930 by the defendants Maxime H. Furlaud and Carlos Reuter of the Duquesne Gas Corporation, of which the plaintiff is the ancillary receiver, and the public issue by defendants of $4,000,000 of bonds and $1,000,000 of notes of said corporation and the sale by them of a part of the stock of said corporation for $850,000.

The facts as found by the District Judge* and which (except as to one detail) are undisputed are, very briefly stated, as follows:

Acting through an incorporated banking house, known as Furlaud & Company (R. 318) which corporation after changing its name was dissolved before the commencement of this suit (R. 333, 155-6), the defendants Furlaud and Reuter caused their banking house to publicly circulate prospectuses covering the issue of the $4,000,000 of bonds and the $1,000,000 of notes, which stated in effect that the proceeds of the issue of these bonds and notes would be used for the purchase of the properties of Duquesne Gas Corporation and for the other corporate purposes of that corporation (R. 326, 263-71, 276-84). The transactions hereinafter related were personally supervised by the defendant Maxime H. Furlaud individually (R. 116, 130, 104,

*The opinion of the District Judge is printed at pages 318-337 of the record.

165). He was the president and chief stockholder of the dissolved corporation Furlaud & Company (R. 165, 157, 158).

Just prior to the issuance of the prospectuses, the defendants procured fraudulent and highly excessive appraisals representing a value of $7,038,000 for the natural gas properties which the Duquesne Gas Corporation was organized to acquire and operate (R. 319-20, 325-6). It was the use of these fraudulent appraisals which made it feasible for the defendants to consummate their fraud upon the Duquesne Gas Corporation and its creditors, the subscribers to the bonds and notes.

It was also found by the District Court that these properties, which cost $2,572,989 or about one-third of the amount of the fraudulent appraisals, were paid for out of the proceeds of the bonds and notes, out of the proceeds of which also came the $365,000 of working capital which, together with the gas properties, was all that the corporation ever received,—and all that its promoters ever intended it should receive,—out of the proceeds of the bonds and notes or for its stock (R. 325-6, 121).

As a result of the issuance of these prospectuses, these defendants through their banking house received $4,492,768.73 from the sale of the bonds and notes, of which they turned over to the Duquesne Gas Corporation or used for its benefit only the sum of $2,937,989.90. They misappropriated and converted to their own use the difference, viz. $1,554,788.83 (R. 325). This sum, with interest computed upon it to the time of the judgment, amounted to the sum of $1,834,640.08, which is the amount of the judgment granted (R. 339).

The corporation at its start had, therefore, an outstanding indebtedness of $5,000,000 represented by $4,000,000

of bonds and $1,000,000 of notes against which it had $2,937,989 of assets consisting of gas properties which cost $2,572,989 and cash working capital of $365,000. Its assets were therefore but 59% of its liabilities. *It was thus insolvent at its very start.*

The public offering was made by the defendants of the $4,000,000 of bonds on March 25, 1930 (R. 258). When about 75 or 80 per cent. of the bonds had been subscribed and the distribution of the bonds was an assured success (R. 111), a closing was arranged to be held at the Central Hanover Bank and Trust Company in New York on April 9, 1930.

Preparations for the closing had been made so as to have the muniments of title of the various gas properties executed and lodged in escrow in various banks in or near Pittsburgh, with provisions that sight drafts covering the purchase prices of the several properties would be lodged in correspondent banks in New York and that, upon the acceptance of such drafts covering the purchase price of the several optioned properties, the title deeds, which ran direct to Duquesne Gas Corporation, would be delivered to the representatives of the promoters (R. 117-119).

It was also arranged by the defendants that the subscribers to the bonds, consisting of forty or fifty distributing houses situated from the Atlantic to the Pacific coast, should have their representatives at the closing to take their bonds to which they had subscribed against payment by certified check (R. 119, 130).

This plan went off according to schedule.

Defendant Furlaud arranged with the Central Hanover Bank and Trust Company for a one day loan or credit, under the bank's strict control, upon the security of the $4,000,000 of bonds and $1,000,000 of notes which were

physically present at the closing (R. 130, 131). Telegraphic assurances were then sent of the acceptances of the sight drafts (R. 118). The mortgages securing the bonds and notes which had been executed were in the hands of the defendants' representatives in Pennsylvania and were thereupon immediately recorded along with the instruments of conveyance which were released from escrow by the Pennsylvania banks pursuant to the telegraphic notice of the acceptance of the drafts (R. 118). The certified checks which were received in payment of the subscriptions of the purchasers of the bonds were thereupon taken and the bonds delivered to the purchasers. A large queue of bank messengers was present and was kept waiting until about the end of the closing which occupied the larger part of the day (R. 105, 119, 130). The money thus received from the bondholders was then immediately applied toward the liquidation of the one day loan (R. 131).

The transactions at the closing were related by three witnesses who attended at the closing, namely: Krog, a former employe of the defendants, whom the defendants made vice-president of Duquesne Gas Corporation for the purpose of signing the bonds and notes and the other corporate records prepared by the defendants (R. 104-105); Duke, who was the attorney in charge of the proceedings at the closing (R. 116-122); and Osborne, who was the officer of the Central Hanover Bank and Trust Company representing the bank at the closing (R. 130-1). These several witnesses all testified to the effect above related and there is no evidence to controvert their testimony.

The opinion of the District Judge correctly sets forth the transactions at the closing.

The defendants created an elaborate set of corporate records in which they used six wholly owned dummy cor-

porations, viz.: Furlaud & Co. (dissolved), Kingston Corporation, Byron Corporation, Chaucer Corporation, Virgil Corporation and Kipling Corporation. These records were, in much, inconsistent with the actual transactions which transpired at the closing. To the extent that they were thus inconsistent with the actual facts these corporate records were fictitious.

The opinion of the Circuit Court of Appeals, seemingly, looks at the fictitious corporate records and overlooks the actual transactions which transpired at the closing and thus falls into a vital error in stating at several places in its opinion that, at the time of the closing, the defendants "owned all of the issued common capital stock of the Duquesne Gas Corporation and all of its bonds and notes." The opinion of the Circuit Court of Appeals is itself inconsistent with the foregoing quoted statement, for its opinion says that on the day of the closing the purchasers of the bonds, to the extent of about $2,350,000 in face amount, paid at the closing by certified check amounts, aggregating $1,886,330. It appears, therefore, from the Circuit Court of Appeals' opinion that bondholders, other than the defendants, to the extent of at least $2,350,000 in face amount had become such at the time of the closing and had then paid at least $1,886,330 which was used to pay for the gas properties then under option for the corporation.

The only material fact as to which there could be said to be conflicting testimony was as to the amount paid in at the closing by the innocent subscribers to the bonds. The plaintiff's proof showed that at the time of the closing the $4,000,000 bond issue had been subscribed to the extent of about 75 or 80 per cent. (R. 111), which, since the price was 96½ (R. 169), would go to show that

about $3,000,000 was paid in at the closing. The opinion of the District Judge so finds (R. 324). The defendants' sole witness Halporn testified to the above figures referred to in the opinion of the Circuit Court of Appeals. The Trial Judge did not choose to believe Halporn but chose rather to believe the other witnesses. The whole testimony of the witness Halporn (R. 162-182) demonstrates that it was quite proper for the Trial Judge to find as he did.

Presumptively, the Trial Court's findings were correct. *Kimberly* v. *Arms,* 129 U. S. 512, 524; 32 L. ed. 764, 769, 1889; *Brookheim* v. *Greenbaum,* 225 F. 763, C. C. A. 2nd 1915; *Dunn* v. *Trefry,* 260 F. 147, C. C. A. 1st 1919; *Benedict* v. *Setters,* 261 F. 492, C. C. A. 8th 1919; *Lackner* v. *McKechney,* 2 F. (2d) 516 C. C. A. 7th 1924; cert. denied 267 U. S. 601, 69 L. Ed. 808; *United States* v. *Mammoth Oil Co.,* 14 F. (2d) 705, C. C. A. 8th 1926, aff'd 275 U. S. 13, 72 L. Ed. 137.

The Appellate Court, although stating the facts quite differently from the findings of the Trial Court, nevertheless made no attempt to demonstrate that any of the findings were erroneous. Nor could such a demonstration have been made, for the reason that the undisputed evidence (except, possibly, as to the amount paid in by the bondholders at the closing) compelled the findings which were made by the Trial Court. Also the omissions of the Appellate Court's opinion as to important facts are, well-nigh, as serious as its misstatements. The Appellate Court reversed upon a false hypothesis.

The presumption of the correctness of the Trial Court's findings should be entertained in this Court notwithstanding the reversal by the Appellate Court.

Mason v. *U. S.*, 260 U. S. 545, 556; 67 L. Ed. 396, 400 (1923);
Adamson v. *Gilliland*, 242 U. S. 350, 353; 61 L. Ed. 356, 358 (1917).

Certainly, the Trial Court's findings upon the undisputed facts are unchallengeable. Whether or not the amount paid in at the closing by the bond subscribers, was, as found by the Trial Court, considerably larger, it is conceded by all that at least $2,350,000 in face amount of bonds had been subscribed for prior to that time and that at least $1,886,330 was then paid in by the subscribers, and that additional subscriptions were coming in daily, and that the whole $4,000,000 bond issue was subscribed and within a few weeks paid for in full by the subscribers.

The bonds were not issuable by the Duquesne Gas Corporation until the day of the closing. This is so for the simple reason that the corporate property was not conveyed to the corporation or the mortgage securing the bonds recorded until that date, at which time a very large amount of the bonds were delivered to the various innocent subscribers against payment in cash. These moneys were used to pay for the corporate properties in order thus to procure the conveyances to the corporation. This procedure required that the whole transaction be part of a simultaneous closing. There is not the slightest room for the conception, therefore, that the defendants ever owned, even for a moment, the bonds which were delivered to and paid for by the innocent subscribers at the time of the closing.

Apart from that, the securities of the Duquesne Gas Corporation, which is a Pennsylvania corporation, were void in the hands of the defendants under the constitution of that Commonwealth and the decisions of the Courts of

that Commonwealth and of the Federal Courts. *Art 16, Sec. 7 of the Constitution of the Commonwealth of Pennsylvania; Commonwealth* v. *Reading Traction Co.*, 204 Pa. 151, 53 A. 755; *Guarantee T. & T. Co.* v. *Dilworth Coal Co.*, 235 Pa. 594 (1912); *Bingaman* v. *Commonwealth Trust Co.*, 15 Fed. (2d) 119 (D. C. M. D. Pa. 1926); *In re Wyoming Valley Ice Co.*, 153 Fed. 787 (D. C. M. D. Pa. 1907); *Gearhart* v. *Standard Steel Co.*, 223 Pa. 385 (1909).

The million dollars of notes, above referred to, were received by the defendants at the closing without the payment of any consideration. The note prospectus, contained statements similar to the statements contained in the bonds to the effect that the proceeds of the issue were to be used for the purchase of properties of the Duquesne Gas Corporation and otherwise for the benefit of the corporation (R. 278, 280, 283). A few weeks after the successful flotation of the $4,000,000 of bonds, the notes were sold by the defendants for $861,097.69 in cash (R. 271, 108, 137).

Since the defendants had received as the proceeds of the bond issue the net sum of $3,631,671.04 (R. 136-7) and had misappropriated for their own use from such proceeds all but the purchase price of the properties which was $2,572,989 (R. 244) and the working capital which was $365,000 (R. 121), namely, they had then misappropriated $693,682.04, the sole purpose of the issuance of the notes was merely for the defendants to misappropriate the whole proceeds thereof which amount to $861,097.69.

This made the total misappropriation by the defendants of the proceeds of the bonds and notes $1,554,779.73. This amount with interest thereon, amounting in all to $1,834,640.08, was the basis of the judgment which the District Court awarded to the plaintiff (Final Decree, R. 339).

The defendants also received at the closing, without the payment of any consideration, 675,000 shares of the capital stock of the corporation 85,000 shares of which they sold through two dummy corporations, the defendants Byron Corporation and Chaucer Corporation, for the sum of $850,000 cash. This sale was made as an outright sale to a stock operator named Bergen (R. 137, 289). There was no proof as to what the defendants did with the remaining 590,000 shares of the capital stock. The denial by the District Court of the plaintiff's claim that defendants were also accountable for this sum of $850,000 constitutes the basis of the plaintiff's cross-appeal. The essential facts in respect of the handling by the defendants of this stock are sufficiently set forth in the opinion of the District Judge.

The Circuit Court of Appeals based its reversal upon the authority of the decision of the United States Supreme Court in *Old Dominion Copper Company* v. *Lewisohn* (C. C. A. Opinion page 7), 210 U. S. 206, 52 L. Ed. 1025. The Circuit Court of Appeals did not refer to or discuss the decision of the United States Supreme Court in *Davis* v. *Las Ovas*, 227 U. S. 80, 57 L. Ed. 426.

THE QUESTIONS PRESENTED

(1) Are the defendants entitled to immunity from accountability to the corporation under the authority of *Old Dominion Copper Company* v. *Lewisohn*? Is not the instant case distinguishable from the *Lewisohn* case?

(2) Does not the instant case fall within the authority of the *Davis* v. *Las Ovas* case instead of the *Lewisohn* case so as to make the defendants accountable to the corporation for the proceeds of the securities of the corporation which were received by them, because, at the closing of

the transaction for the purchase of the property, the very money of innocent subscribers for the bonds was applied to the payment for the corporate properties?

(3) Since the corporation was, through the fraudulent acts of the defendants rendered insolvent at its start, has not the plaintiff, in his capacity as receiver and standing in the right of the creditors, the right to disaffirm the acts of the corporation?

(4) Did not the statements which the defendant Furlaud caused to be inserted in both the bond and note prospectuses, to the effect that the proceeds thereof were to be devoted to the purposes of the corporation, constitute such representations as to the purpose for which the proceeds of the bonds and notes were to be used as to impress a trust upon such proceeds for the benefit of the Duquesne Gas Corporation?

(5) Was not the Duquesne Gas Corporation powerless, even with the consent of all of its stockholders, directors and officers, to render itself insolvent by surrendering to the defendants its right to hold them accountable to it for the proceeds which came into the hands of the defendants from the issuance of its securities?

(6) Is not the individual defendant Maxime H. Furlaud accountable in the place and stead of Furlaud & Company, since the defendant Furlaud individually supervised and conducted the transactions and caused Furlaud & Company which he dominated to make the wrongful misappropriations and breach of trust and thereafter cause the corporation Furlaud & Company, to be dissolved before the commencement of this suit?

REASONS FOR THE ALLOWANCE OF THE WRIT

(1) The decision of the Circuit Court of Appeals is clearly erroneous and most inequitable and unjust. The decision of the Supreme Court in *Old Dominion Copper Company* v. *Lewisohn* is not, as the Circuit Court of Appeals seems to hold, authority for the granting of immunity from accountability to the defendants as the promoters of the corporation for their fraudulent misappropriations, breaches of trust and secret profits. The instant case is distinguishable from the Supreme Court's decision in the case of *Old Dominion Copper Company* v. *Lewisohn* and more properly falls within the authority of the Supreme Court's later decision in *Davis* v. *Las Ovas*. This latter decision limits the scope of the case of *Old Dominion Copper Company* v *Lewisohn*. The Circuit Court of Appeals did not refer to the decision of the Supreme Court in the case of *Davis* v. *Las Ovas*, and it seems therefore that the Circuit Court of Appeals overlooked the proper effect to be given to that decision.

(2) Although the Circuit Court of Appeals, Second Circuit, in its decision in the case of *Ball* v. *Breed*, 294 Fed. 227, to which it also refers in its opinion herein as authority, applied *Old Dominion Copper Company* v. *Lewisohn* as authority for granting to promoters immunity from accountability, the Federal Courts in other Circuits have been more inclined to look upon the Supreme Court's decision in *Davis* v. *Las Ovas* as limiting the decision of *Old Dominion Copper Company* v. *Lewisohn*, and in several instances the Federal Courts in other Circuits have held promoters accountable to the corporation under the authority of *Davis* v. *Las Ovas* rather than as immune from accountability under the authority of *Old Dominion Copper*

Company v. *Lewisohn*. See: *Tilden* v. *Barber*, 268 Fed. 587 (D. C. N. J. 1920); *American Shipbuilding Co.* v. *Commonwealth S. S. Co.*, 215 Fed. 296 (C. C. A. 6th, 1914); *Dunlap* v. *Twin City Power Co.*, 226 Fed. 161 (C. C. A. 4th, 1915); *Humble Oil Co.* v. *Campbell*, 69 Fed. (2d) 667 (C. C. A. 5th, 1934). In other Federal cases referring to *Old Dominion Copper Company* v. *Lewisohn*, in which the promoters have been held not accountable, such as: *Ball* v. *Breed supra; South Penn Collieries Co.* v. *Sproul*, 52 Fed. (2d) 557, 561 (C. C. A. 3rd, 1931); *Johnson* v. *Louisville Trust Co.*, 293 Fed. 857, 861 (C. C. A. 6th, 1923), the decisions seem to be based more upon the fact that in those cases, the promoters' profits were not excessive or secret.

IMPORTANCE OF THE QUESTIONS

It is most important that this Court review the decision of the Circuit Court of Appeals, which seems to hold that the decision in *Old Dominion Copper Company* v. *Lewisohn* compels a determination that the defendants are entitled to immunity from accountability for their fraudulent acts as the promoters of the corporation in misappropriating the proceeds of the corporate securities. Reference to the reported decisions in both the federal and state courts shows that the Supreme Court's decision in *Old Dominion Copper Company* v. *Lewisohn* has been frequently invoked by fraudulent promoters as a shield against accountability, and, in some cases other than the instant case, has been applied with that effect (See Appendix). Even the District Judge, though impressed as his opinion shows with the grossly fraudulent character of the transactions, felt constrained by *Old Dominion Copper Co.* v. *Lewisohn* to hold defendants immune from account-

ability for the $850,000 received by them as the proceeds of a part of the stock.

It is to be feared that the decision of the Circuit Court of Appeals, if permitted to stand, will be taken as an authoritative interpretation of the *Old Dominion* case as a precedent that fraudulent promoters are immune from accountability even in grossly fraudulent transactions, such as those presented by the instant case.

It is important, therefore, that the Court should review the decision of the Circuit Court of Appeals in order to clarify the application of the *Old Dominion Copper Company* v. *Lewisohn* decision.

WHEREFORE, it is respectfully submitted that this petition for a writ of certiorari to review the decision of the Circuit Court of Appeals of the Second Circuit dated the 11th day of March, 1935 and the decree of the United States District Court for the Southern District of New York, dated the 11th day of May 1933, should be granted.

GEORGE W. MCCANDLESS,
as Ancillary Receiver of Duquesne Gas Corporation,

By RALPH ROYALL,
WILLIAM A. MAGEE and
CLARK MILLER,
Counsel for Petitioner.

April, 1935.

BRIEF IN SUPPORT OF PETITION

OPINIONS OF THE COURTS BELOW

The opinion of the District Court is reported in 4 Fed. Supp. 884 (Advance Sheets only) and is printed at pages 318-37 of the record. The first opinion of the Circuit Court of Appeals is reported in 68 Fed. (2d) 925. The opinion of the United States Supreme Court upon the prior appeal is reported in 79 Law. Ed. 32. The second opinion of the Circuit Court of Appeals is not yet reported.

JURISDICTION

The jurisdiction to issue the writ is found in Sec. 240-a of the Judicial Code as amended by the Act of February 13, 1925, c. 299, Sec. 1, 43 Stat. 938; Sec. 347-a of Title 28, U. S. C.

STATEMENT OF FACTS

The statement of facts set out in the foregoing petition is hereby adopted and is supplemented as follows:

The bond prospectus issued by the defendants contained the following:

"SECURITY

The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, aggregate $7,038,000 (R. 266).

* * * * * * *

CAPITALIZATION

	Authorized	Outstanding
First Mortgage 6% Convertible Gold Bonds (this issue)	$4,000,000	$4,000,000
Convertible 6½% Secured Gold Notes	1,000,000	1,000,000
Common Stock (no par value)	1,250,000 Shs.	675,000 Shs.

(R. 267)

* * * * * * *

PURPOSE OF ISSUE

These bonds are issued by the Corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes" (R. 270).

The note prospectus contained similar statements under similar captions (R. 277-284).

SPECIFICATION OF ERRORS

1. The Circuit Court of Appeals erred in reversing the decree dated the 11th day of May, 1933, and in dismissing the complaint.

2. The Circuit Court of Appeals erred in refusing to modify the decree dated the 11th day of May, 1933, by adding to the amount of the judgment against defendants Furlaud and Kingston Corporation the sum of $850,000 with interest, and directing that judgment also be entered against defendants Byron Corporation and Chaucer Corporation in the sum of $425,000 with interest.

ARGUMENT

I

The prospectuses plainly were intended to induce the belief in those whose subscriptions to the bonds and notes were solicited that, not only the whole net proceeds of the bond and note issues were to be made available by the bankers to the corporation for the acquisition of the corporate properties and for working capital and other corporate purposes, but that in addition the 675,000 shares of issued stock represented some very substantial contribution to capital of not less than the difference between the $5,000,000 represented by the bonds and notes and the $7,038,000 stated by the prospectus to constitute the assets.

Corporate bonds are, of course, not looked upon favorably unless there is some equity in the property beyond the amount of funded debt. It is quite apparent that the whole prospectus was designed to convey the belief that the corporation was set up with a real capital of $7,000,000 and that, therefore, not only the whole proceeds of the bonds and notes, but some very substantial amount representing the outstanding stock was to be made available to the corporation.

These prospectuses must be interpreted according to the impression which they convey rather than upon a too narrow and literal construction. *Aaron's Reefs* v. *Twiss* (L. R. App. Cas. 1896), 273, 285, opinion of Lord Halsbury; *Downey* v. *Finucane*, 205 N. Y. 251; *Gates* v. *Megargel*, 266 Fed. 811.

Certainly, the prospectuses were not intended to induce the belief in those whose subscriptions for the

bonds and notes were solicited that the proceeds of these issues were to a large extent to be misappropriated by the promoters, and that the new corporation was actually to receive less than $3,000,000 from the issuance of all its securities, and thus be hopelessly insolvent at the start. The bondholders and noteholders must have intended that the proceeds of their subscriptions were to be used for the benefit of the corporation. The defendants well knew this, for the simple reason that the prospectuses which they issued induced in the subscribers to the bonds and notes this belief.

Where one delivers money to another with the intention that that other shall pay the money to a third person, a trust arises which may be enforced by that third person. *McKee* v. *Lamon,* 159 U. S. 317, 322; *Sayer* v. *Wynkoop,* 248 N. Y. 54; 2 Storey's Equity Juris. (12th Ed.), Sec. 1255; 26 R. C. L. 1235, Sec. 82.

The corporation's beneficial interest in the proceeds of the bonds and notes constituted a property right which the corporation was powerless, even with the consent of all its stockholders, directors and officers, to give away, thus rendering the corporation insolvent. Fletcher Cyclopedia of Corporations, Permanent Edition, Sec. 7407.

The stockholders may not take the corporate assets even as against prospective creditors, and, in such circumstances the receiver or trustee of the corporation may recover. *Coleman* v. *Tepel,* 230 Fed. 63, 71 (C. C. A. 3rd, 1916).

The misappropriation by the defendants of a large part of the proceeds of the bonds and notes was a conversion of the property of the corporation, and a fraud upon its creditors. The receiver has the right to recover for this conversion of the corporate funds.

It is a distortion of the case of *Old Dominion Copper Company* v. *Lewisohn* to treat it as the Circuit Court of Appeals did, as authority for the granting of immunity from accountability for this wrongful misappropriation.

Although no representations were made in respect to the stock such as were made in respect of the bonds and notes from which a trust for the corporation arose, nevertheless the courts below erred in not also awarding additional judgment to the plaintiff for the sum of $850,000 received by the defendants as the proceeds of the sale of part of the stock.

The relation of the defendants,— the promoters—to the corporation, was of a fiduciary character. *Yeiser* v. *United States Board & Paper Co.*, 107 Fed. 340 (C. C. A. 6th, 1901); *Humble Oil Co.* v. *Campbell*, 69 Fed. (2d) 667 (C. C. A. 5th, 1934).

Even assuming that the defendants owned all of the capital stock of the corporation at the time of the closing of the transaction, still, in the situation presented by the instant case, they were not free to deal with the corporation as they wished, and as though it were their own.

Where, as here, the corporation is created as an insolvent corporation by its promoters, the position of the creditors overshadows the position of the stockholders.

In the instant case there were bondholders to the extent of at least $2,350,000 in face amount,—the Trial Court found there were considerably more,—who had become such at the time of the closing.

The theory of *Old Dominion Copper Company* v. *Lewisohn* case is summed up in two sentences of the Supreme Court's opinion (210 U. S. 212):

> "At the time of the sale to the plaintiff, then, there was no wrong, to anyone. Bigelow, Lewisohn,

> and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in exchange for their conveyance of their land."

This indicates the deep and wide distinction between that case and the instant case. In the instant case defendants were not upon both sides of the bargain. On the other side of the bargain at the time of the closing were the creditors of this insolvent corporation; namely the bondholders who had become such at the time of the closing. Furthermore, the stock of the corporation was not in the instant case exchanged for a conveyance by the defendants of their property. In fact, no property of the defendants was exchanged for the stock. The property here involved was paid for directly to the original owners with the proceeds of the bonds and notes.

Old Dominion Copper Company v. *Lewisohn* has been distinguished and limited by the later decision in *Davis* v. *Las Ovas Co.*, 227 U. S. 80; 57 L. Ed. 426. In the latter case the property was purchased by a syndicate and resold to the corporation. Unknown to some of their associates in the syndicate the promoters obtained an option to purchase the property for themselves at a lower price, with the result that the corporation was required to pay a secret profit to the promoters. The Supreme Court held that, as the innocent members of the syndicate were to become stock subscribers and directors of the company, the buyers and sellers were not the same, and that the distinction between this and a case in which all of the owners of the property and all of the members of the buying corporation are the same persons and participate in the profit was fully recognized in the *Lewisohn* case. The Supreme Court affirmed a judgment in favor of the plaintiffs. The case is

clear authority for the proposition that the rule of the *Lewisohn* case applies only where there are no innocent persons involved at the time of the transaction, that is when all parties in interest participate in the profit. This court also pointed out that the corporate right of action was not defeated by the fact that the recovery would inure to the benefit of the guilty as well as the innocent. The court also said:

> "The standing of the corporation results from the fact that there were innocent and deceived members of the corporation when the property was taken over by it."

Certainly the instant case presents a much stronger case than *Davis* v. *Las Ovas* for the application of the doctrine of that case. In the instant case the payment over to the corporation of the defendants' whole secret profit will redound wholly to the defrauded creditors of this insolvent corporation.

Certainly, the plaintiff herein as receiver stands in the rights of these creditors. *Casey* v. *Cavaroc*, 96 U. S. 467, 488; *Atlantic Trust Co.* v. *Chapman*, 208 U. S. 360.

The *Las Ovas* case and the cases following it generally deal with situations in which there were innocent stockholders.

The case of *Johnson* v. *Louisville Trust Company*, 293 Fed. 857, 861 (C. C. A. 6th, 1923), as well as some other cases which have applied the *Old Dominion* v. *Lewisohn* case suggest that the existence of innocent creditors is sufficient. The Court said, speaking of the *Las Ovas* rule:

> "* * * such rule would scarcely seem applicable * * * for nothing seems to have been done to mislead or deceive prospective creditors."

The cases of:

Hoffman Motor Truck Co. v. *Erickson,* 124 Minn. 279 (1914);

Inland Nursery & Floral Co., v. *Rice,* 57 Wash. 67 (1910);

Vasey v. *Coal Co.,* 89 W. Va. 499 (1921);

Coleman v. *Tepel,* 230 Fed. 63, 71 (C. C. A. 3rd, 1916).

are to similar effect.

There is much to be said, broadly speaking, for such a suggestion. On the other hand there is authority to the contrary, such as the case of *Allenhurst Park Estates* v. *Smith,* 101 N. J. Eq. 581 (1927), which is cited in the opinion of the Circuit Court of Appeals.

But, in respect of an *insolvent* corporation, there is, we submit only one possible view open to a Court of Equity. In the case of such a corporation the creditors have the sole interest in the affairs of the corporation. The interest of the stockholders is purely technical and formal. The case of *Allenhurst Park Estates* v. *Smith,* and any others to similar effect, which we have seen are cases in which the corporation was amply solvent.

It is unthinkable that the Courts of Equity should countenance a view that promoters may deal as they please with the corporations in their control, even to the extent of misappropriating the creditors' money and rendering the corporation insolvent. As stated by the Trial Court

> "* * * simple justice requires that the receiver, in his representative capacity, should be able to vindicate the rights of creditors who were victimized. If

> a court of equity is to function within the domains of conscience, and if it is to redress the wrongs that occur within that dominion, it must provide a remedy that is capable of check-mating the ingenuity that here perpetrated a grievous wrong." (Opinion of Judge Knox, R. 333.)

These defendants did not have the least right to appropriate any of these securities, or the proceeds of them, and should have been held accountable for all. This conclusion follows general rules which are well recognized in Courts of Equity and is reenforced by Art. 16 Sec. 7 of the Pennsylvania constitution which makes all of these securities void in the hands of these defendants.

II

The individual defendant Maxime H. Furlaud was properly held by the District Court to be accountable for the misappropriated moneys. He personally arranged and supervised the transactions. Although the affairs for which he was held responsible by the Trial Court were to a large extent carried on in the name of Furlaud & Company, Maxime H. Furlaud was nevertheless the president and chief stockholder of that corporation and dominated it. After the fraudulent misappropriations were committed, the individual defendant Maxime H. Furlaud caused that corporation first to change its name and then to dissolve.

One may not cause a corporation which is under his dominion to commit a breach of trust without himself becoming accountable for the consequences. *Anderson* v. *Daley*, 38 App. Div. 505 (Appeal dismissed 159 N. Y. 146).

CONCLUSION

It is submitted that it is most important that this Court should review the application of its decision in *Old Domin-*

ion Copper Company v. *Lewisohn* with respect to situations, such as the instant one, in which fraudulent promoters and bankers claim,—under what they assert to be a correct construction of that case,—immunity from accountability for fraudulent misappropriation. It is also submitted that the decision of the Circuit Court of Appeals is most inequitable and unjust and that the writ should be granted.

Respectfully submitted,

RALPH ROYALL,
WILLIAM A. MAGEE and
CLARK MILLER,
Of Counsel.

APPENDIX

The decision in *Old Dominion Copper Mining and Smelting Company* v. *Lewisohn*, 210 U. S. 206 (1908), and the other decisions of the Federal and State Courts since that time dealing with the subject.

The litigation growing out of the promotion of the Old Dominion Copper Mining and Smelting Company took a varied course. The corporation itself (there was no receivership) brought two suits which, except as to the defendants named, were identical. One was the suit instituted in the Federal court in New York against Lewisohn, one of the alleged fraudulent promoters, which resulted in the determination by the Supreme Court in 210 U. S. 206. The other was a suit brought in the State courts of Massachusetts against Bigelow, who was Lewisohn's associate as promoter. The Supreme Court of the United States held that the corporation had no right of action against its promoters to recover for a secret profit, since they owned all the stock of the corporation at the time of the transaction and were thus on both sides of the bargain, even though it was contemplated at the time that others should become stockholders by original subscription without knowledge of the secret profit. The Supreme Court of the State of Massachusetts (203 Mass. 159) reached the directly opposite conclusion. In a suit brought in New Jersey seeking to enjoin the corporation from pursuing Bigelow, the Supreme Court of New Jersey (74 N. J. Eq. 457) preferred to take the view of the Massachusetts court; and the United States Supreme Court itself in a later decision, 225 U. S. 111 (1912) refused to require the Massachusetts court to conform to the Supreme Court's decision. Thus

while one of the joint promoters of the Old Dominion Company escaped liability in the Federal courts, his fellow promoter was finally held liable by the Massachusetts courts.

These suits and the several phases of them in the United States, Massachusetts and New Jersey courts are reported as follows:

188 Mass. 315 (1905);
203 Mass. 159 (1909);
74 N. J. Equity 457 (1908);
136 Fed. 915 (1905);
210 U. S. 206 (1908);
225 U. S. 111 (1912);
195 Fed. 637 (1911);
202 Fed. 178 (1913).

The two latest decisions above referred to in the Federal courts involved a continuation of the same action after amendments to the complaint had been made. A brief history of the several suits and decisions growing out of the transaction is given by Judge Hough in 195 Fed. 637 (1911). Although Judge Noyes in the Circuit Court of Appeals (202 Fed. 178) indicated that he thought the amended complaint stated a cause of action in spite of the previous decision of the Supreme Court of the United States, recovery was denied on principles of estoppel and *res adjudicata*. (Writ of Cert. denied, 229 U. S. 613 (1913).)

The Supreme Court subsequently clarified and strictly limited the general application of the doctrine of the *Lewisohn* case in *Davis* v. *Las Ovas Co.*, 227 U. S. 80 (1913). There one of the members of a syndicate, organized for the promotion of a corporation, made a secret profit in the trans-

action, thus injuring the other members of the syndicate who also were to become stockholders. It was held that a right of action for this fraud vested in the corporation. It was further held that the corporate right of action could not be defeated by the fact that the recovery would inure to the benefit of the guilty as well as the innocent. The Court made it clear that the *Lewisohn* case should not be applied in situations in which any innocent parties are affected. It is to be especially noted that in this case the Supreme Court referred with particular approval to the decision made by the Circuit Court of Appeals of the 6th Circuit in the year 1901, in the case of *Yeiser* v. *U. S. Board & Paper Co.*, 107 Fed. 340 (C. C. A. 6th, 1901), as well as to the leading English case of *New Sombrero Phosphate Co.* v. *Erlanger*, L. R. 5 Chan. Div. 73. The Supreme Court said at page 87:

> "The distinction between a case in which all of the owners of the property and all of the members of the buying corporation are the same persons, and participate in the profit realized, and the case here presented, is fully recognized in *Old Dominion Copper Mining & Smelting Co.* v. *Lewisohn*, as well as in *New Sombrero Phosphate Co.* v. *Erlanger*, L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rep. 436, and in the well-considered opinion of Judge Severens in *Yeiser* v. *United States Board & Paper Co.*, 52 L. R. A. 724, 46 C. C. A. 567, 107 Fed. 340."

The extent of the limitation placed by the *Las Ovas* case upon the *Old Dominion* case is shown by the following language from the "well considered opinion of Judge Severens in *Yeiser* v. *United States Board & Paper Co.*," which the Supreme Court adopts as shown by the quotation above. Judge Severens says (107 Fed. 340, 344):

> "It is a well-settled principle of equity that those who participate in bringing about the organization of an incorporated company, and in getting it in condition for transacting the business for which it is organized, assume the obligations of a *trustee* towards the company and *those who shall be invited* to come into the enterprise as stockholders and share in ~~its~~ fortunes."

The English case of *New Sombrero Phosphate Co.* v. *Erlanger*, which as shown above, was expressly approved by the Supreme Court of the United Staets in *Davis* v. *Las Ovas*, was a case in which the promoters owned all the stock of the corporation at the time they made a secret profit on the sale of property to the corporation. The concealment in the prospectus sent to its future security holders was held to give the corporation a right of action for the fraud. Jessel, *M.R.* said at page 112:

> "Now, understanding, as I do, that the promoters of a company stand in a fiduciary relation to that company which is their creation; in this case that is emphatically so, for up to this time there was not really a single *bona fide* shareholder distinct from the promoters."

and on page 123:

> "* * * the syndicate, as promoters, being in a fiduciary relation to the company, it was essential that the public, who were invited to become, and who were expected to become, the shareholders of the company, and to constitute the company, should have the fullest information as to all the surrounding circumstances."

Since the *Lewisohn* case was decided by the Supreme Court fraudulent promoters have attempted many times to

invoke its doctrine in order to escape liability. The Federal courts as a rule, however, have distinguished that case and followed the *Davis* v. *Las Ovas* case. The following are such cases:

In *Tilden* v. *Barber,* 268 Fed. 587 (D. C. N. J. 1920), the promoters were held liable to the corporation though they owned all the stock at the time of the transaction with the corporation. This result was reached on the theory that the promoters were in the position of trustees to subscribers who were to be future stockholders of the corporation. The court at page 598 quoted the foregoing language from *Yeiser* v. *U. S. Board & Paper Co.*

The Court of Appeals in the 6th Circuit again invoked this trust doctrine in *American Shipbuilding Co.* v. *Commonwealth S.S. Co.,* 215 Fed. 296 (C. C. A. 6th, 1914). It was there said that when the promoters commenced their negotiations for the organization of the company, they were acting as trustees for the future corporation and its stockholders. The same result was reached in *Dunlap* v. *Twin City Power Co.,* 226 Fed. 161 (C. C. A. 4th, 1915).

In *Humble Oil Co.* v. *Campbell,* 69 Fed. (2d) 667 (C. C. A. 5th, 1934), which is the latest decision of the Federal courts upon the subject, the defendant issued and sold certificates of interest in certain oil properties owned by him and represented that all the proceeds would be turned over to the unit holders. In violation of the trust thus created the defendant sold a portion of the property and retained the proceeds. A corporation was organized to take over the property and the unit holders subsequently became shareholders in the corporation. In this suit by the receiver of the corporation it was contended that, under the doctrine of the *Lewisohn* case, no right of action existed in favor of the receiver. But the court held that the defend-

ant occupied a fiduciary relation to the unit holders and the future corporation, that where such a relationship exists the corporation may follow and gather in the trust property in spite of the rule of the *Lewisohn* case.

The Federal cases which applied the *Lewisohn* case in denying a recovery by the corporation, can, we believe, be distinguished on the ground that no fraud was actually practised by the promoters. These are the cases of *Ball* v. *Breed*, 294 Fed. 227, 231 (C. C. A. 2d, 1923); *South Penn Collieries Co.* v. *Sproul*, 52 Fed. 2d 557, 561 (C. C. A. 3rd, 1931); *Johnson* v. *Louisville Trust Co.*, 293 Fed. 857, 861 (C. C. A. 6th, 1923).

The question involved in the *Old Dominion* cases has arisen many times in the State courts of the country. The State courts have frequently discussed the conflict between the Massachusetts decision in the *Bigelow* case and the U. S. Supreme Court decision in the *Lewisohn* case and in most cases have preferred to follow the Massachusetts decision or the Supreme Court's *Las Ovas* decision. Such cases are the following:

Calif. *California Mining Co.* v. *Wells*, 170 Calif. 285 (1915);

Ken. *Datillo* v. *Roaten Creek Oil Co.*, 222 Ky. 378 (1927);

Maine *Land Co.* v. *Lewis*, 101 Me. 78 (1905);

Mich. *Torrey* v. *Toledo Portland Cement Co.*, 158 Mich. 348 (1909);

American Forging Co. v. *Wiley*, 206 Mich. 664 (1919);

N. J. *Arnold* v. *Searing*, 78 N. J. Eq. 146 (1910);

Bigelow v. *Old Dominion Copper Mining & Smelting Co.*, 74 N. J. Eq. 457;

Ore. *Wills* v. *Nehalem Coal Co.*, 52 Ore. 70 (1908);
Rugger v. *Mt. Hood Electric Co.*, 143 Ore. 193 (1933);
R. I. *Anderson* v. *Johnson*, 45 R. I. 17 (1923);
S. D. *Meier* v. *Eaton*, 46 S. D. 286 (1923);
Wisc. *Pittsburg Mining Co.* v. *Spooner*, 74 Wisc. 307 (1889);
Pietsch v. *Milbrath*, 123 Wisc. 647 (1905);

See also:

Ariz. *Frame* v. *Mahoney*, 21 Ariz. 282 (1920);
Conn. *Yale Gas Stove Co.* v. *Wilcox*, 64 Conn. 101 (1894);
Ga. *Downey* v. *Byrd*, 171 Ga. 532 (1930);
Mo. *South Joplin Land Co.* v. *Case*, 104 Mo. 572 (1891);
Pa. *Densmore Oil Co.* v. *Densmore*, 64 Pa. St. 43 (1870).

Such, also, is the view of the English Courts:

New Sombrero Phosphate Co. v. *Erlanger*, L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rp. 436 (opinion of Jessel, *M.R.*);
Gluckstein v. *Barnes* (1900) App. Cas. 240 (opinion of Lord Macnaghten).

Only a few of the states have indicated a preference for the *Lewisohn* decision.

See:

Colo. *Lilylands Canal Co.* v. *Wood*, 56 Colo. 130 (1913);

Minn. *Hoffman Motor Truck Co.* v. *Erickson,* 124 Minn. 279 (1914);

Wash. *Inland Nursery & Floral Co.* v. *Rice,* 57 Wash. 67 (1910);

W. Va. *Vasey* v. *Coal Co.,* 89 W. Va. 499 (1921).

But even in those jurisdictions which have approved the rule of the *Lewisohn* case, the courts have recognized that, where the rights of creditors are involved, the result may be different. See particularly:

Hoffman Motor Truck Co. v. *Erickson,* 124 Minn. 279 (1914);

Inland Nursery & Floral Co. v. *Rice,* 57 Wash. 67 (1910);

Vasey v. *Coal Co.,* 89 W. Va. 499 (1921);

Johnson v. *Louisville Trust Co.,* 293 Fed. 857, 861 (C. C. A. 6th, 1923).

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CHARLES ELMORE CRO

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of DUQUESNE GAS CORPORATION,

Petitioner,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER GEORGE W. McCANDLESS AS RECEIVER OF DUQUESNE GAS CORPORATION

RALPH ROYALL
WILLIAM A. MAGEE
CLARK MILLER
Of Counsel.

September, 1935.

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Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of DUQUESNE GAS CORPORATION,
Petitioner,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR PETITIONER GEORGE W. McCANDLESS AS RECEIVER OF DUQUESNE GAS CORPORATION

This case comes before the Court on writ of certiorari granted to the United States Circuit Court of Appeals for the Second Circuit, on the 13th day of May 1935 (79 L. Ed. 841).

The suit was brought in the District Court of the United States for the Southern District of New York where a decree was rendered on May 11, 1933, awarding a judgment to the plaintiff in the sum of $1,834,640.08 (R. 233). Said decree was reversed by the judgment of the Circuit Court of Appeals for the Second Circuit filed January 15, 1934 (R. 256) on the ground that the appoint-

ment of the plaintiff as ancillary receiver was void and he therefore did not have capacity to sue.

The Supreme Court granted a writ of certiorari on April 30, 1934 (78 L. Ed. 863) limited, however, to the question of the validity of the appointment of the plaintiff as ancillary receiver, and upon the appeal pursuant to such writ the Supreme Court reversed said judgment of the Court of Appeals, dated January 15, 1934, and remanded the case to the Court of Appeals for reargument and for the determination of the questions relating to the liability of the defendants decided by the District Court and presented by the appeal and cross-appeal (79 L. Ed. 32).*

Upon the rehearing pursuant to the mandate of the Supreme Court, the Circuit Court of Appeals rendered a judgment, dated March 11, 1935, reversing the judgment of the District Court on the whole case (R. 273). The writ of certiorari granted by the Supreme Court on May 13, 1935, brings up for review this last mentioned determination of the Court of Appeals.

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*The opinion of the Circuit Court of Appeals, by Manton, Circuit Judge, upon the rehearing erroneously states in the second paragraph thereof (R. 262):

> "A receiver was appointed for the Duquesne Gas Corporation in the United States District Court for the Western District of Pennsylvania, and he sued in the District Court for the Southern District of New York, without appointment therein as an ancillary receiver. We reversed the decree, on a former appeal, for failure to have an ancillary receiver appointed in the Southern District of New York before suit (68 Fed. 2, 925). The Supreme Court reversed (79 Law Ed. 32) remanding the cause to this court to pass upon the merits of the issues presented."

The opinion of the Supreme Court (79 L. Ed. 32) put the reversal upon the ground that the validity of the appointment of the plaintiff as ancillary receiver could not be raised for the first time upon appeal. The Supreme Court was far from deciding that a foreign equity receiver can sue.

PREVIOUS OPINION OF THIS COURT AND OPINIONS BELOW

The opinion of the District Court is printed at page 218 of the record, and is reported in 4 Fed. (2d) 884 (Advance Sheets only). The opinion of the Court of Appeals on the first reversal is printed at page 251 of the record and is reported at 68 Fed. (2d) 925. The opinion of the Court of Appeals upon the second reversal is printed at page 261 of the record and is reported at 75 Fed. (2d) 977. The previous opinion of this Court is reported at 79 L. Ed. 32, 293 U. S. 67.

JURISDICTION

Jurisdiction arises from the granting of the writ of certiorari herein pursuant to Section 240 (A) of the Judicial Code as amended by the Act of 1925.

STATEMENT

We will divide the statement into three parts, (1) the actual facts, (2) the fictitious corporate records, and (3) the treatment of the facts by the Court of Appeals.

The Actual Facts

The subject matter of the suit is the promoting in 1930 by the defendant Maxime H. Furlaud and his associate Carlos Reuter (the latter was named as a defendant but not served with process) of the Duquesne Gas Corporation, of which the plaintiff is the ancillary receiver, and the public issue by defendants of $4,000,000 of bonds and $1,000,000 of notes of said corporation and the sale by them of a part of the stock of said corporation for $850,000.

The facts as found by the District Judge* and which (except as to one detail) are undisputed are, very briefly stated, as follows:

---

*The opinion of the District Judge is printed at pages 218-232 of the record.

Furlaud and Reuter acted through an incorporated banking house, known as Furlaud & Company (R. 219) which corporation after changing its name was dissolved before the commencement of this suit (R. 229, 109). They caused their banking house to publicly circulate prospectuses covering the issue of the $4,000,000 of bonds and the $1,000,000 of notes, which stated in effect that the proceeds of the issue of these bonds and notes would be used for the purchase of the properties of Duquesne Gas Corporation and for the other corporate purposes of that corporation (R. 224, 183-8, 192-9).† The transactions hereinafter related were personally supervised by the defendant Maxime H. Furlaud (R. 81, 91, 71, 116). He was the president and chief stockholder of the dissolved corporation Furlaud & Company (R. 116, 110, 111).

Just prior to the issuance of the prospectuses, the defendants procured a fraudulent and highly excessive ap-

---

†The relevant part of the prospectuses which are to this effect read as follows:

"SECURITY

The appraisals of the engineers covering the properties of the Corporation, including working capital of $365,000, aggregate $7,038,000 (R. 266).

* * * * * * * * * * * *

CAPITALIZATION

	Authorized	Outstanding
First Mortgage 6% Convertible Gold Bonds (this issue)	$4,000,000	$4,000,000
Convertible 6½% Secured Gold Notes	1,000,000	1,000,000
Common Stock (no par value)	1,250,000 Shs.	675,000 Shs. (R. 267)

* * * * * * * * * * * *

PURPOSE OF ISSUE

These bonds are issued by the Corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes" (R. 270).

The note prospectus contained similar statements under similar captions (R. 277-284).

praisal stating a value of $7,038,000 for the natural gas properties (including $365,000 working capital) which the Duquesne Gas Corporation was organized to acquire and operate (R. 219-20, 224). The most improper methods pursued by the promoters in obtaining this appraisal are set out in the opinion of the District Court (R. 219, 220). Illustrative of this is the fact that the witness Nuss, who was one of the vendors and an expert oil and gas man familiar with such properties in the district and with fair market values, in addition to the property which he sold made a pure gift to the corporation of a contingent royalty lease on an undeveloped tract of 14,000 acres. This was included in this fraudulent appraisal at $840,000 (R. 61). It was through the use of this fraudulent appraisal that the defendants were able to consummate their fraud upon the Duquesne Gas Corporation and its creditors, the subscribers to the bonds and notes.

It was also found by the District Court that these properties, which cost $2,572,989 (Ptfs. Ex. 11, R. 170A) or about one-third of the amount of the fraudulent appraisal, were paid for out of the proceeds of the bonds and notes, out of the proceeds of which also came the $365,000 of working capital. That was all that the corporation ever received,—and all that its promoters ever intended it should receive,—out of the proceeds of the bonds and notes or for its stock (R. 224, 84).

Thus, while these defendants through their banking house received $4,492,768.73 from the sale of the bonds and notes (R. 95) they turned over to the Duquesne Gas Corporation or used for its benefit only the sum of $2,937,-989.90 (R. 78). They misappropriated and converted to their own use the difference, viz. $1,554,788.83 (R. 224). This sum, with interest, amounted to the sum of $1,834,-

640.08, which is the amount of the judgment granted (R. 233, 234).

The corporation at its start had, therefore, an outstanding indebtedness of $5,000,000 represented by $4,000,000 of bonds and $1,000,000 of notes against which it had $2,937,989 of assets consisting of gas properties which cost $2,572,989 and cash working capital of $365,000. Its assets were therefore but 59% of its liabilities. *It was thus insolvent at its very start.*

The defendants accomplished this fraud in the manner now briefly related.

The public offering of the $4,000,000 of bonds was made by the defendants on March 25, 1930 (R. 180). When about 75 or 80 per cent. of the bonds had been subscribed and the distribution of the bonds was an assured success (R. 76), a closing was arranged to be held at the Central Hanover Bank and Trust Company in New York on April 9, 1930.

Before arranging for the closing, the defendants had paid to the several vendors comparatively small sums aggregating a total of $45,510 (R. 170A) to make binding the options which until then were gratuitous. Preparations for the closing were then made so as to have the muniments of title of the various gas properties which were to be acquired by the corporation executed and lodged in escrow in various banks in or near Pittsburgh, with provisions that sight drafts covering the purchase prices of the several properties would be lodged in correspondent banks in New York and that, upon the acceptance of such drafts covering the purchase prices of the several optioned properties, the title deeds, which ran direct to Duquesne Gas Corporation, would be delivered to the representatives of the promoters (R. 81-82).

It was also arranged by the defendants that the subscribers to the bonds, consisting of about thirty distributing houses situated all over the United States, should have bank messengers at the closing to take the bonds for which they had subscribed against payment by certified check (R. 74, 82, 91).

This plan went off according to schedule.

Defendant Furlaud arranged with the Central Hanover Bank and Trust Company for a one day loan, upon the security of the bonds and notes all of which were physically present at the closing. As testified by the bank's officer Osborne "The bank always had a string on the money" (R. 91). Telegraphic assurances were then sent of the acceptances of the sight drafts (R. 81). The mortgages securing the bonds and notes which had been executed were in the hands of the promoters' representatives in Pennsylvania and were thereupon immediately recorded along with the instruments of conveyance which were released from escrow by the Pennsylvania banks pursuant to the telegraphic notice of the acceptance of the drafts (R. 82). The certified checks which were received in payment of the subscriptions of the purchasers of the bonds were thereupon taken and the bonds delivered to the purchasers. A large queue of bank messengers was present and was kept waiting until about the end of the closing which occupied the larger part of the day (R. 72, 82, 91). The money thus received from the bondholders was immediately applied toward the liquidation of the one day loan (R. 91).

These transactions at the closing were related by three witnesses who attended at the closing, namely: Krog, a former employe of the defendants, whom the defendants made vice-president of Duquesne Gas Corporation for the purpose of signing the bonds and notes and the other cor-

porate records prepared by the defendants (R. 71, 72); Duke, who was the defendants' attorney in charge of the proceedings at the closing (R. 81-84); and Osborne, who was the officer of the Central Hanover Bank and Trust Company representing the bank at the closing (R. 91). There is no evidence to controvert their testimony.

The balance of the bonds, the entire million dollars of notes and 675,000 shares of the capital stock, were appropriated by defendants at the closing without the payment of any consideration (R. 82, 83, 84). The balance of the bonds were soon sold (R. 95, 129).

A few weeks after the successful flotation of the $4,000,000 of bonds, the notes were sold by the defendants for $861,097.69 in cash (R. 189, 75, 95, 223).

Since the defendants had received as the proceeds of the bond issue the net sum of $3,631,671.04 (R. 95, 223) and had misappropriated for their own use from such proceeds all but the purchase price of the properties which was $2,572,989 (R. 170A) and the working capital which was $365,000 (R. 84), namely, they had then misappropriated $693,682.04, *the sole purpose of the issuance of the notes was merely for the defendants to misappropriate the whole proceeds thereof which amounted to $861,097.69.*

This made the total misappropriation by the defendants of the proceeds of the bonds and notes $1,554,779.73, above mentioned.

Of the 675,000 shares of the capital stock of the corporation which the defendants appropriated 85,000 shares were soon after sold through two dummy corporations, the defendants Byron Corporation and Chaucer Corporation, for the sum of $850,000 cash. This sale was made as an outright sale to a stock operator named Bergen (R. 96, 200, 201.). There was no proof as to what the defendants did with the remaining 590,000 shares of the capital stock. The

denial by the District Court of the plaintiff's claim that defendants were also accountable for this sum of $850,000 constituted the basis of the plaintiff's cross-appeal to the Court of Appeals.

The Fictitious Corporate Records

After the taking of the corporate proceedings which were had immediately before the closing to increase the capital stock from 1,000 shares to 1,250,000 shares, to authorize and approve the form of the $4,000,000 bond issue and the form of the mortgage securing the bonds and the $1,000,000 note issue and the form of the note indenture (R. 205-210, 211-217), a straightforward record of the actual transactions would have been a simple one. Since the purchase price of the gas properties, which cost $2,572,989 plus the $365,000 of working capital, was to be financed out of the proceeds of the $4,000,000 bond issue, and the balance of the proceeds of the bond issue amounting to nearly $700,000 and the whole proceeds of the $1,000,000 note issue and the whole proceeds of the issued 675,000 shares of stock, were to be appropriated by the promoters, this could have been recorded in a straightforward one page corporate resolution to that effect.

But such a record would for the purposes of the promoters have made too clear the nature of the transactions, so they chose instead to attempt to camouflage the facts through the use of an elaborate and confusing set of corporate proceedings containing five large volumes of minutes of the Duquesne Gas Corporation (R. 199) besides endless legerdemain recorded on the books of their dummy corporation Kingston Corporation and the four other dummy corporations euphoniously called Byron Corporation, Chaucer Corporation, Virgil Corporation and Kipling Corporation (R. 109-112, 200, 201, 203).

After recording the authorization, etc., of the increase of the capital stock and the making of the bond issue and of the note issue, they then recorded a so-called "Reorganization Agreement" dated April 7, 1930 between Duquesne Gas Corporation and Kingston Corporation which in effect purported to provide that Kingston Corporation was to turn over to Duquesne Gas Corporation the gas properties in consideration of $3,015,000 cash, $1,300,000 in face amount of Duquesne bonds and 535,000 shares of Duquesne stock (R. 201-203). They also recorded at the same time the making by Furlaud & Company, Inc. to Duquesne Gas Corporation and the acceptance by the latter of an offer to purchase $2,700,000 of bonds at 90, $1,000,000 of notes at 88, and 139,000 shares of stock at 50c a share, making a total of $3,379,500 (R. 206-207, 209-210).

At the closing, which was held at the Central Hanover Bank and Trust Company two days after the day of the record of these corporate proceedings, they went through the following forms: Maxime H. Furlaud arranged for the opening of two so-called one day credits, one running to Kingston Corporation in the amount of $3,015,000 and the other running to Furlaud & Company, Inc. in the amount of $3,379,500 (R. 91, 117, 119). These so-called one day credits were liquidated on that day and there was not a moment when the bank did not have a string upon the money (R. 91). They then on that day had Furlaud & Company, Inc. go through the form of delivering a check to Duquesne for the $3,379,500 and at the same moment had Duquesne deliver a check to Kingston Corporation for $3,015,000 (R. 78, 200). The difference of $364,500, together with the $500 which had been previously subscribed by the promoters for the 1,000 original shares, made the $365,000 of working capital which was left in the Duquesne treasury (R. 78).

The drafts which were taken up at that time covering the balance of the purchase price then payable under the escrow agreements, amounting to $2,449,900 (R. 84) were charged to the one day credit opened as above stated in the name of Kingston Corporation (R. 81). But this credit was immediately liquidated in full by the passing from Duquesne to Kingston of the $3,015,000 check, so that there was left a net balance to the credit of Kingston in the amount of $565,100 (R. 176). This $565,100 just fell off the table and into the pockets of Furlaud & Company, Inc. for on that day Kingston Corporation passed two checks to Furlaud & Company, Inc. aggregating $565,100 (R. 117).

The Distributing Group letter which Furlaud & Company, Inc. had already sent out under date of March 19th stated that it had purchased the whole $4,000,000 bond issue (R. 178). The way they recorded the transaction was that Furlaud had purchased $2,700,000 of the bond issue (R. 209-210) and that Kingston had acquired the other $1,300,000 (R. 201-203). The record which they made showed that this $1,300,000 of bonds remained in the Kingston Corporation until June 4th when it was made the subject of a so-called "dividend in kind" (R. 100), and this notwithstanding the fact that long before June 4th substantially the whole $4,000,000 had been issued and sold to innocent subscribers. The record also showed that Furlaud & Company, Inc. had purchased the $2,700,000 of bonds at 90, $1,000,000 of notes at 88 and 139,000 shares of stock at 50c a share, making an aggregate purchase price of $3,379,500 (R. 206-207, 209-210), which was pure fiction.

If Furlaud & Company, Inc. could be said to have purchased these securities at all, the purchase price was $3,379,500, less $565,100 which they received back on the

same day, or an aggregate purchase price of $2,814,400. If, as they claim, they purchased $2,700,000 of bonds at 90 or for $2,430,000, there was left of the total purchase price of $2,814,000 but $384,400 as the purchase price of the notes and stock. But they had the corporate minutes recite that they were purchasing the $1,000,000 of notes at 88 or $880,000, and the 139,000 shares of stock at 50c a share. The various corporate records which they created are not only inconsistent with the irrefutable facts but are inconsistent with one another.

It is, of course, manifest that the $3,015,000 figure written into the so-called "Reorganization Agreement" and the $3,379,500 figure written into the so-called Furlaud purchase of securities were purely arbitrary figures chosen because when subtracting one from the other a difference of $364,500 remained which as above stated produced, together with the $500 theretofore subscribed by the original incorporators, the specified working capital of $365,000 (R. 78). Any arbitrary figures which produced a difference of $364,500 would have served as well.

The further records they made in respect to the handling of the stock emphasize the fictitious character of the transactions. As above stated, they recorded the acquisition by Kingston Corporation of 535,000 shares of stock and by Furlaud & Company, Inc. of 139,000 shares of stock, which together with the 1,000 shares of stock which they recorded as subscribed for by the original incorporators made the total 675,000 shares of issued stock. As a matter of fact, the whole 675,000 shares of stock, when issued, were placed in the name of one Parisette who was an employee of Furlaud & Company, Inc. and bore a sort of *caveat* stamp that the shares could not be transferred without the consent of Furlaud (R. 91-92).

They then drew the Byron Corporation and the Chaucer Corporation into the recording of the stock transactions by recording on the minutes of these corporations that in one case the wife of Carlos Reuter (R. 101) and in another case an employee of Furlaud's (R. 102) had acquired valuable options for the purchase of some of this stock from Kingston Corporation which these optionees were willing to turn over to the Byron Corporation and Chaucer Corporation, respectively, and that the Byron Corporation and Chaucer Corporation were to exercise these options and give their promissory notes for the purchase price at 50c a share (R. 101, 102).

They then entered into an agreement with one J. J. Bergen, a stock operator, making the agreement in the name of Byron Corporation and Chaucer Corporation, for the sale of 85,000 shares at $10 a share, making an aggregate purchase price of $850,000 for the joint and equal account of these two dummy corporations to the extent of $425,000 each (R. 95-97, 100).

The dummy Virgil Corporation and Kipling Corporation were drawn into the records apparently for no other purpose than to put some nic[illegible]wists and turns in the trail (R. 105, 106, 109).

We submit that these devious and fictitious corporate records cannot alter the indisputable facts as to the realities of the situation, but serve merely to emphasize and aggravate the fraudulent character of the whole transaction.

The Treatment of the Facts by the Court of Appeals

Judge Manton's opinion, seemingly, looks at the fictitious corporate records and overlooks the actual transactions which transpired at the closing and the Court of Appeals thus falls into a vital error in stating that, at the time of the closing, the defendants "owned all of the issued com-

mon capital stock of the Duquesne Gas Corporation and all of its bonds and notes" (R. 268). The opinion is itself inconsistent with the foregoing quoted statement, for it says that on the day of the closing the purchasers of the bonds, to the extent of about $2,350,000 in face amount, paid at the closing by certified check amounts, aggregating $1,886,330 (R. 266). It appears, therefore, from the Court of Appeals' opinion that bondholders, other than the defendants, to the extent of at least $2,350,000 in face amount had become such at the time of the closing and had then paid at least $1,886,330 which was used to pay for the gas properties.

The only fact as to which there could be said to be conflicting testimony was as to the amount paid in at the closing by the innocent subscribers to the bonds. The plaintiff's proof showed that at the time of the closing the $4,000,000 bond issue had been subscribed to the extent of about 75 or 80 per cent. (R. 76), which, since the price was 96½ (R. 119), would go to show that about $3,000,000 was paid in at the closing. The opinion of the District Judge so finds (R. 223). The defendants' sole witness Halporn mentioned the above figures referred to in the opinion of the Court of Appeals, but admitted (R. 119) that this was of uncertain accuracy.

Even if the testimony of Halporn were believed, the conclusion that the defendants owned all of the bonds at the time of the closing is wholly unwarranted. It is conceded by all that at least $2,350,000 in face amount of bonds had been subscribed for prior to that time and that at least $1,886,330 was then paid in by the subscribers.

The bonds could not have been issued by the Duquesne Gas Corporation until the day of the closing. This is so for the simple reason that the corporate property was not conveyed to the corporation or the mortgage securing the

bonds recorded until that date, at which instant a very large amount of the bonds were delivered to the various innocent subscribers against payment by them in cash. These moneys were used to pay for the corporate properties in order thus to procure the conveyances to the corporation. This procedure required that the whole transaction be part of a simultaneous closing (R. 81-85). There is not the slightest room for the conception, therefore, that the defendants ever owned, even for a moment, the bonds which were delivered to and paid for by the innocent subscribers at the time of the closing.

The Court of Appeals (R. 266, 7) seems to attach importance to the fact that on the day of the closing Furlaud & Company, Inc. had also negotiated loans with three other banks aggregating $1,500,000. It is a fact that the defendants' witness Halporn testified to that effect, and that these loans were secured by the bonds, notes and stock of Duquesne Gas Corporation (R. 114). To what extent recourse was had to these loans at the time of the closing depends upon how much the bondholders paid in at the closing, which Halporn testified was $1,886,330 (R. 128). This sum was more than two-thirds of all that was required at the closing to pay for the corporate properties and to furnish the stipulated working capital.*

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*Amount used at the closing to pay for the corporate properties and to furnish the stipulated working capital (Testimony of Duke (R. 84)):

For the properties	$2,449,900
For working capital	364,500
	$2,814,400
Amount received at the closing from the innocent bond subscribers (Testimony of Halporn (R. 128))	1,886,330
Balance required for the closing	$ 928,070

As shown by the findings of the Trial Court (R. 223), the Court did not regard Halporn's testimony as credible in all respects, especially his minimizing version as to the extent to which these various loans were liquidated at the closing through the use of the moneys then furnished by the innocent bond subscribers. What amount, if any, may have been required to be furnished by the other three banks in order to carry out the closing was at best an arrangement lasting but for a few days for the reason that bond subscriptions continued to come in daily (R. 129), so that the balance required must have soon been made up from that source. Since their loans were upon the security of the

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The following is an analysis of the Furlaud & Co., Inc. one day loan account at Central Hanover Bank:

Amount credited on April 9th to Furlaud & Company, Inc.'s account at Central Hanover Bank representing certified checks received from innocent bond subscribers (R. 128)	$1,886,330
Amount credited to Furlaud & Company, Inc.'s account at Central Hanover Bank which came around back on April 9th by way of Kingston Corporation (R. 117, 128)	565,100
Amount credited on April 9th to Furlaud & Company, Inc.'s account at Central Hanover Bank as the proceeds of loans from the three lending banks (R. 114)	1,500,000
	$3,951,430
Amount of one day loan to Furlaud & Company, Inc. by Central Hanover (R. 117)	3,379,500
Balance to credit of Furlaud & Company, Inc. on April 9th after the payment of the $3,379,500 one day loan	$ 571,930

This balance was immediately turned over to the accounts of Furlaud & Company, Inc. at the three lending banks (R. 118). Halporn testifies (R. 118) that this balance was $482,782.02. But clearly this was a misstatement. It is apparent that, after crediting against the loans of $1,500,000 of the three lending banks, the balance of $571,930, the moneys furnished for the purposes of the closing by the three lending banks, could not have exceeded the difference between $1,500,000 and $571,930, which makes the above figure of $928,070.

bonds, notes and stock of this insolvent corporation (R. 114), these banks too must have been deceived and innocent parties.

But not to make too fine a point of it, it is entirely sufficient for the purposes of this case that the defendants conceded that the innocent bond subscribers had furnished at least $1,886,330 at the closing to this insolvent corporation and that this money was used by the promoters in acquiring the corporate properties direct from the original owners. In no possible view of the facts were the promoters as stated by the Court of Appeals alone upon both sides of the bargain.

The Appellate Court, although stating the facts quite differently from the findings of the Trial Court, nevertheless made no attempt to demonstrate that any finding was erroneous. Nor could such a demonstration have been made, for the reason that the undisputed evidence (except as to the amount paid in by the bondholders at the closing) compelled the findings which were made by the Trial Court. The Appellate Court reversed upon a false hypothesis.

The error of the Court of Appeals arises chiefly from its misstating a vital fact, viz.: that at the time of the closing the defendants "owned all of the issued Common capital stock of the Duquesne Gas Corporation and all of its bonds and notes," and then proceeding upon the theory that, under this view of the facts, the judgment should be reversed upon the authority of the decision of the United States Supreme Court in *Old Dominion Copper Company* v. *Lewisohn*, 210 U. S. 206, 52 L. Ed. 1025 (1908). The Court of Appeals did not refer to or discuss the decision of the United States Supreme Court in *Davis* v. *Las Ovas*, 227 U. S. 80, 57 L. Ed. 426 (1912).

SPECIFICATION OF ERRORS—SUMMARY OF ARGUMENT

1. The Court of Appeals erred in disregarding the findings of the District Court, which were based upon clear, ample and undisputed testimony, and in basing its reversal upon a false hypothesis as to vital facts.

2. The Court of Appeals erred in not holding that the defendants stood in a fiduciary relation to the corporation and that they were accountable to the corporation as fiduciaries for the proceeds coming into their hands from all of the securities of the corporation.

3. The Court of Appeals erred in not holding that the statements which defendant Furlaud caused to be inserted in both the bond and note prospectuses constituted such representations as to the purposes for which the proceeds thereof were to be used as to impress a trust upon such proceeds for the benefit of the corporation.

4. The Court of Appeals erred in not holding that, since the corporation was, by the fraudulent acts of the defendants, rendered insolvent at its start, the plaintiff in his capacity as receiver standing in the right of the creditors had the right to disaffirm the acts of the corporation.

5. The Court of Appeals erred in not holding that the corporation was powerless to render itself insolvent by surrendering to the defendants its right to hold them accountable to it for the proceeds which came into the hands of the defendants from the issuance of the securities of the corporation.

6. The Court of Appeals erred in not holding that in the hands of the defendants all of the securities issued to them were void under the Pennsylvania Constitution, and that the defendants at no time were in the position of stockholders, bondholders or noteholders of the corporation.

7. Since the defendant Furlaud was himself a promoter of the corporation, and since he individually supervised and conducted the transactions and caused the corporation Furlaud & Company, which he dominated, to make the wrongful appropriations and breach of trust, and thereafter caused Furlaud & Company to be dissolved, the Court of Appeals erred in not holding that he was individually accountable and liable for the wrongful appropriation and breach of trust.

8. The Court of Appeals erred in reversing the decree of the District Court.

9. The Court of Appeals erred in failing to modify the decree and increase the amount of the judgment as against defendants Furlaud and Kingston Corporation by adding $850,000 with interest, and by also granting judgment against each of the defendants Byron Corporation and Chaucer Corporation in the amount of $425,000 with interest.

POINT I

PRESUMPTIVELY THE TRIAL COURT'S FINDINGS WERE CORRECT. THE PRESUMPTION OF THE CORRECTNESS OF THESE FINDINGS SHOULD BE ENTERTAINED IN THIS COURT NOTWITHSTANDING THE REVERSAL BY THE COURT OF APPEALS.

The Court of Appeals did not review any of the findings of the District Court, set out carefully in the opinion of the District Court, or make any analysis or examination relating to any of them, or specifically reverse any of them; indeed, except as to one detail, none of the findings could have been, upon a true analysis of the testimony, in any way altered, for the reason that the findings were supported by clear, ample and undisputed testimony.

That one detail concerns the amount of bonds delivered and paid for at the closing by innocent subscribers. The defendants' version of the facts was that $2,350,000 in face amount of the bonds were thus delivered against payment of $1,886,330. The plaintiff's version is that a larger amount of bonds was delivered and paid for. The Trial Court found that about 75% or 80% of the issue had been subscribed for at the time of the closing and about $3,000,000 paid in by the innocent subscribers. This finding was supported by evidence.

Presumptively, the trial court's findings were correct. *Kimberly* v. *Arms,* 129 U. S. 512, 524; 32 L. ed. 764, 769, (1889); *Brookheim* v. *Greenbaum,* 225 Fed. 763, (C. C. A. 2nd 1915); *Dunn* v. *Trefry,* 260 Fed. 147, (C. C. A. 1st 1919); *Benedict* v. *Setters,* 261 Fed. 492, (C. C. A. 8th 1919); *Lackner* v. *McKechney,* 2 Fed. (2d) 516, (C. C. A. 7th 1924); cert. denied 267 U. S. 601, 69 L. Ed. 808; *United States* v. *Mammoth Oil Co.,* 14 Fed. (2d) 705, (C. C. A. 8th 1926); aff'd. 275 U. S. 13, 72 L. Ed. 137.

The presumption of the correctness of the trial court's findings should be entertained in this court notwithstanding this reversal by the Court of Appeals. *Mason* v. *U. S.,* 260 U. S. 545, 556; 67 L. Ed. 396, 400 (1923); *Adamson* v. *Gilliland,* 242 U. S. 350, 353; 61 L. Ed. 356, 358 (1917).

But even if the Appellate Court had seen fit upon a review of the evidence to reject the Trial Court's finding upon this fact and in place thereof to adopt the version of the defendants, nothing can justify the vital misstatement contained in the opinion of the Court of Appeals that at the time of the closing the defendants "owned all of the issued Common capital stock of the Duquesne Gas Corporation and all of its bonds and notes."

POINT II

THE DEFENDANT FURLAUD AS THE PROMOTER OF THE CORPORATION STOOD IN A FIDUCIARY RELATION TO IT SO AS TO BE ACCOUNTABLE FOR THE WHOLE PROCEEDS OF THE SECURITIES OF THE CORPORATION WHICH WERE DIVERTED AND MISAPPROPRIATED.

The Duquesne Gas Corporation was the creature of Furlaud. He caused the corporation to be organized. All of its capital stock was issued to one Parisette, his nominee, and the directors and officers were his nominees (R. 210, 211, 220).

As shown by the statement of facts, at the time of the closing of the transaction between the promoter and the corporation, about 75 or 80 percent of the $4,000,000 of bonds of the corporation were outstanding in the hands of innocent holders. The amount of their paid-in subscriptions thereto aggregated about $3,000,000. The balance of the whole $4,000,000 bond issue was then in the course of being subscribed to by innocent holders, and these additional subscriptions were soon after paid in full. In addition to this the promoter then contemplated an issue of $1,000,000 of notes which were soon after put into the hands of innocent purchasers, and for which the promoter received the additional sum of $861,097.69. Of the proceeds of these two issues, the promoter appropriated $1,554,779.73, and put into the corporation merely the gas properties, which cost $2,572,989, and $365,000 working capital, with the result that the corporation had at its start $2,937,989 of assets against a funded debt of $5,000,000. Its assets were, therefore, 59% of its liabilities, and it was insolvent at its creation.

As Judge KNOX puts it (R. 227):

> "At their (Furlaud's and Reuter's) behest and procurement, the gas corporation acted as it did. It was they who inflicted upon it the congenital injury that stunted its growth and circumscribed its life."

The mere fact that at the time of the closing the promoter had caused to be issued to his nominee all of the issued capital stock of the corporation did not, under these circumstances, permit the promoters to deal with the corporation as they pleased, and even to appropriate the proceeds of the corporation's securities to such an extent as to render it hopelessly insolvent.

It must be that under circumstances such as these the promoter is to be regarded as standing in a fiduciary relation to the corporation.

Yeiser v. *United States Board & Paper Co.*, 107 Fed. 340, 344 (C. C. A. 6th 1901). Judge SEVERENS says:

> "It is a well-settled principle of equity that those who participate in bringing about the organization of an incorporated company, and in getting it in condition for transacting the business for which it is organized, assume the obligations of a trust towards the company and those who shall be invited to come into the enterprise as stockholders and share in its fortunes."

New Sombrero Phosphate Co. v. *Erlanger*, L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rep. 436 (1877). JESSEL M. R. says at L. R. 5 Ch. Div. 112:

> "Now, understanding, as I do, that the promoters of a company stand in a fiduciary relation to that company which is their creation; in this case that is emphatically so, for up to this time there was not really

> a single *bona fide* shareholder distinct from the promoters."

and on page 123:

> "* * * the syndicate, as promoters, being in a fiduciary relation to the company, it was essential that the public, who were invited to become, and who were expected to become, the shareholders of the company, and to constitute the company, should have the fullest information as to all the surrounding circumstances."

The Supreme Court in *Davis* v. *Las Ovas*, 227 U. S. 80, 87, 57 L. Ed. 426, 430 (1913), commented upon these two decisions with approval and referred to "the well-considered opinion of Judge SEVERENS."

Perhaps the matter cannot be put more trenchantly than in the language of LORD MACNAGHTEN, writing for the House of Lords, and holding the promoters liable at the suit of a receiver in *Gluckstein* v. *Barnes* (1900), App. Cas. 240:

> "It is the old story. It has been done over and over again. * * * These gentlemen set about forming a company to pay them a handsome sum for taking off their hands a property which they had contracted to buy with that end in view. They bring the company into existence by means of the usual machinery. They appoint themselves sole guardians and protectors of this creature of theirs, half-fledged and just struggling into life, bound hand and foot while yet unborn by contracts tending to their private advantage, and so fashioned by its makers that it could only act by their hands and only see through their eyes. They issue a prospectus representing that they had agreed to purchase the property for a sum largely in excess of the amount which they had, in fact, to pay. On the faith of this prospectus they collect subscriptions from a confiding and credulous public. And then comes the last act. Secretly, and therefore dishonestly, they put into

their own pockets the difference between the real and the pretended price. After a brief career the company is ordered to be wound up."

But the Court of Appeals holds that this fraudulent promoter is entitled to immunity from liability or accountability under the authority of the decision of the United States Supreme Court in the case of *Old Dominion Copper Company* v. *Lewisohn,* 210 U. S. 206, 52 L. Ed. 1025 (1908).*

In this case the promoters, having acquired property with their own moneys, organized a corporation which took over their property in exchange for all of the securities of the corporation then issued, which consisted wholly of stock. Later they had the corporation sell a comparatively small number of shares to furnish working capital. These shares were sold at a substantially higher price than the cost to the promoters of the shares which had been issued

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*The litigation involving the liability of its promoters to Old Dominion Copper Company, of which the suit resulting in this decision is a part, had a remarkable history. It arose also in other suits dealing with the same subject matter in the Courts of Massachusetts and New Jersey, as well as in the suit entitled *Bigelow* v. *Old Dominion Copper Company,* which was decided in the Supreme Court in 1912, 225 U. S. 111, 56 L. Ed. 1009. In the Massachusetts case, the Supreme Court of that state declined to follow the decision of the Supreme Court of the United States but affirmed a final judgment holding the fellow promoter of Lewisohn accountable to the corporation for the whole secret profit, while the United States Supreme Court, in its decision in 225 U. S. above referred to, refused to require the Massachusetts Court to conform to the United States Supreme Court's decision in the *Lewisohn* case and the New Jersey Court refused to enjoin the Old Dominion Copper Company from continuing to pursue the co-promoter Bigelow in the Massachusetts Court in disregard of the United States Supreme Court's decision in the *Lewisohn* case.

For the convenience of the Court, we have set out in an appendix a brief history of this litigation with citation of the cases commenting upon it which have been since decided in the Federal and State Courts.

to them. The theory of the decision is, we submit, summed up in two sentences of the Court's opinion (210 U. S. 212):

> "At the time of the sale to the plaintiff, then, there was no wrong done to anyone. Bigelow, Lewisohn, and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in exchange for their conveyance of their land."

The case holds that owners of property may organize a corporation to take over their property on such terms as they please, provided that no one but they have an interest in the corporation, or, as the Court puts it, if they are on both sides of the bargain.

But in the instant case the defendants were not upon both sides of the bargain. At the moment of the consummation of the fraud upon this insolvent corporation these innocent and deceived bondholders were on the other side of the bargain.

In the case of *Davis* v. *Las Ovas, supra,* the Supreme Court's previous decision was distinguished and limited. In the *Davis* case the Supreme Court referred to the *Old Dominion* decision as follows (227 U. S. 86):

> "It is then said: 'If we admit, for the purposes of this point, that appellants did deceive some of the syndicate, what has the company to do with it? For this they cite *Old Dominion Copper Min. & Smelting Co.* v. *Lewisohn,* 210 U. S. 206, 52 L. ed. 1025, 28 Sup. Ct. Rep. 634, where it was held that a subordinate fraud practised by some of the promoters of a corporation upon some of their associates was a matter wholly between them and the syndicate, which gave rise to no corporate right of action in the absence of innocent incorporators or stockholders.'"
>
> "But that is not this case. Some of those, if not all, interested by appellants in the property and in its purchase for a proposed consideration were ignorant

of the real price which they were to pay for it, and were not, therefore, in complicity with their scheme to make a secret profit. These innocent members of the syndicate became stock subscribers and directors of the company, as did appellants. The buyers and sellers were not the same. Those of the syndicate assuming to act for the corporation in acquiring the property were under obligation to disclose the truth and deal openly. In the absence of such disclosure the corporate assent was obtained on false grounds. The wrong was done when those members of the syndicate not in complicity with appellants subscribed to the stock of the company and aided their guilty associate managers in the corporate action necessary to the corporate acquisition of the property at the exaggerated price placed upon it by those who were to realize a secret profit. Thus, the original fraud practised upon some of those associated with them in the promoters' arrangement became operative against the corporation itself. The standing of the corporation results from the fact that there were innocent and deceived members of the corporation when the property was taken over by it."

These two decisions of the Supreme Court when read together clearly establish that it is enough to make the promoters accountable to the corporation for their secret profit that other parties interested in the corporation did not share in the profit and were without knowledge of it; and that this result follows, even though the promoters had with their own moneys first acquired the property to be put into the corporation which was thereafter turned over at an exaggerated price.

It will be seen then how much stronger is the instant case for the application of such a rule. The corporate property was acquired by the corporation direct from its original owners. On any possible view of the facts, the moneys

of the innocent bondholders constituted at the very moment of the closing much the larger part of the moneys required for the full purchase price of the properties of the corporation and its working capital. Even if, according to the defendants' version of the facts, the innocent bondholders did not at the moment of the closing furnish all the money required for these purposes, it is undisputed that they furnished more than two-thirds of it and that their subscriptions were coming in daily and must within a matter of days have equalled all the capital the corporation ever had, or was intended by the promoters to have, and that soon these subscriptions greatly exceeded the amount required, which excess the promoters simply misappropriated. The corporation was put into being by the promoters with assets equaling but 59% of its liabilities. A stronger situation for applying the principles clearly laid down by the decision in *Davis* v. *Las Ovas* cannot well be imagined.

The Court of Appeals, nevertheless, entirely disregarded this court's *Davis* v. *Las Ovas* decision.

The defendants argued in the Court of Appeals that the decision of the case was governed by the *Old Dominion* case rather than by the *Davis* v. *Las Ovas* case, and that the fact that, at the time of the closing, the defendants, as they claimed, owned all of the capital stock of the corporation was enough to compel a judgment giving immunity to the defendants under the authority of the *Old Dominion* decision. They said it made no difference that there were innocent and deceived bondholders, and that this was so for the reason that bondholders or creditors should not be considered as members of the corporation so as to have the *Las Ovas* case govern the decision. The Court of Appeals on the other hand disposes of this subject by merely proceeding upon the erroneous hypothesis as to the

facts that the defendants were the owners not only of all of the stock, but of all the bonds and notes, as well.

For the argument that the existence of bondholders was of no importance, defendants cited as their chief authority the case of *Allenhurst Park Estates* v. *Smith,* 101 N. J. Eq. 581, 138 Atl. 709 (1927). But in that case it appeared that:

> "The complainant company is perfectly solvent and is not in the hands of a receiver" (138 Atl. 716).

The same is true of the other cases along this line cited by the defendants to the Court of Appeals.

On the other hand, there is authority indicating a different view. The case of *Johnson* v. *Louisville Trust Company,* 293 Fed. 857, 861 (C. C. A. 6th 1923), suggests that the existence of innocent prospective creditors is of some consequence.

There is much to be said for the view that creditors have an interest in the preservation of the corporate fund, even before depredations upon it have created insolvency. However this may be, it simply cannot be the law that the interest which the creditors have in preserving the corporate fund will be overlooked by the Courts when the corporation is rendered insolvent by the fraud perpetrated on it by its promoters. We have found no such decision in the books other than the decision of the Court of Appeals which is here for review, and we do not believe there is any such.

Certainly, in the case of an *insolvent* corporation, innocent creditors who have been injured by the promoters' fraud must be regarded as members of the corporation for the purposes of the *Las Ovas* decision. *In the instant case no one but the creditors furnished a cent of capital to the corporation. Who but they had any interest in this insolvent corporation?* In respect of an insolvent corpora-

tion, the interest of the creditors in the corporate fund is paramount. This is self evident and is shown clearly by the case of *Coleman* v. *Tepel*, 230 Fed. 63, 71 (C. C. A. 3rd 1916):

> "* * * when a stockholder, with the knowledge he has or with that with which he is charged concerning the financial condition of the corporation, engages in a transaction which results in a depletion for his advantage of corporate assets below the subscribed capital or below existing liabilities, as the law may be, and becomes a party to the solvent appearance of a business that is intended to be continued, he is bound by his act both to existing and future creditors, when its direct object or immediate consequence is the insolvency of the corporation and injury to creditors."

If the *Lewisohn* decision has the effect the Court of Appeals gives to it, a method is provided by which promoters may with impunity commit any fraud against the corporation, however flagrant and however much innocent parties whose interests then exist in the corporation may be made to suffer; for then this may be accomplished by the mere device of having the corporation, which can act only by the hands of its promoters, subscribe to a set of records fictitiously reciting that, at the time of the closing of the transaction between the promoters and the corporation, no one but the promoters had an interest in the corporation. This, we submit, is not the meaning of the *Lewisohn* decision.

As to the $850,000 received by the defendants as the proceeds of the sale by them of the shares of stock, although the District Court clearly felt that the whole transaction was most fraudulent, nevertheless that Court felt con-

strained by the Supreme Court's decision in the *Lewisohn* case to hold with the defendants as to this.

But in this the District Court fell into error in overlooking the fiduciary character of the relationship of the promoters to the corporation arising from the fact that at the time of the closing of the transaction innocent persons had a very large interest in the corporation.

The defendants should have been held accountable as fiduciaries for the proceeds of all the securities including the $850,000 which they received as the proceeds of the sale by them of a part of the stock as well as for the appropriation of a large part of the proceeds of the bonds and the whole proceeds of the notes.

POINT III

THE STATEMENTS CONTAINED IN THE BOND AND NOTE PROSPECTUSES WERE SUCH AS TO IMPRESS A TRUST UPON THE PROCEEDS OF THE ISSUE OF THE BONDS AND NOTES FOR THE BENEFIT OF THE CORPORATION.

What we have previously said as to the prospectuses plainly shows that they were intended to induce the belief in those whose subscriptions to the bonds and notes were solicited that the whole net proceeds of the bond and note issues was to be made available by the promoters to the corporation for the acquisition of the corporate properties and for working capital and other corporate purposes. No corporate bond or note is, of course, looked upon favorably unless there is some equity in the property beyond the amount of the funded debt. It is apparent that the whole prospectus was designed to convey the belief that the new corporation was set up with a real capital of over $7,000,000 and that, therefore, not only the whole net proceeds of the

bonds and notes but some very substantial amount representing the outstanding stock was to be made available to it.

The chiefly relevant parts of these prospectuses are quoted at the foot of page 4.

These prospectuses must be interpreted according to the impression which they convey rather than upon a too narrow and literal construction.

Downey v. *Finucane*, 205 N. Y. 251, 264 (1912):

> "Speaking of an equivocal prospectus which was condemned as fraudulent by the House of Lords in *Aaron's Reefs* v. *Twiss* (L. R. [App. Cas. 1896], 273, 285) Lord Halsbury calls the language ambidextrous; and this expression aptly characterizes that in the present case. In the case cited it was argued, as it is suggested here, that there was no specific allegation of fact which is proved to be false; but the lord chancellor protested against this being regarded as the true test and declared that the question was whether taking the whole thing together was there a false representation. 'I do not care by what means it is conveyed—by what trick or device or ambiguous language; all those are expedients by which fraudulent people seem to think they can escape from the real substance of the transaction. If by a number of statements you intentionally give a false impression and induce a person to act upon it, it is not the less false although if one takes each statement by itself there may be a difficulty in showing that any specific statement is untrue.'"

See also: *Gates* v. *Megargel*, 266 Fed. 811 (C. C. A. 2d 1920), citing *Ryan* v. *Ohmer*, 244 Fed. 31, 34 (C. C. A. 2d 1931); *Moran* v. *Standard Oil*, 211 N. Y. 187, 196 (1914).

No more need be said to demonstrate that these prospectuses were not designed to induce the belief in those

whose subscriptions for the bonds and notes were solicited that the proceeds of these issues were to a large extent to be misappropriated by the promoters and that the new corporation was actually to receive considerably less than $3,000,000 from the issuance of all of its securities and thus be hopelessly insolvent at its creation. On the contrary the bondholders and noteholders must have intended that the proceeds of their subscriptions were to be used for the benefit of the corporation, as the promoters, who had taken pains to induce that belief, well understood.

Where one delivers money to another with the intention that that other shall pay the money to a third person, a trust arises which may be enforced by that third person.

McKee v. *Lamon,* 159 U. S. 317, 322, 40 L. Ed. 165 (1917):

> *"There can be no doubt of the general proposition that where money is placed in the hands of one person to be delivered to another, a trust arises in favor of the latter, which he may enforce by a bill in equity,* if not by action at law. The acceptance of the money with notice of its ultimate destination is sufficient to create a duty on the part of the bailee to devote it to the purposes intended by the bailor. *Taylor* v. *Benham,* 46 U. S. 5 How. 233, 274; *Kane* v. *Bloodgood,* 7 Johns. Ch. 110, 11 Am. Dec. 417; *Baring* v. *Dabney,* 86 U. S. 19 Wall. 1; *National Bank of Baltimore* v. *Connecticut Mut. L. Ins. Co.,* 104 U. S. 54; *Keller* v. *Ashford,* 133 U. S. 610; *Union Mut. L. Ins. Co.* v. *Hanford,* 143 U. S. 187; *Ryan* v. *Dox,* 34 N. Y. 307, 90 Am. Dec. 696; Story, Eq. Jur. §§1041, 1255; Mechem, Agency, §568. * * *
>
> "The objection that there was no consideration for the promise made by the appellant to adjust the claims of all parties, etc., is untenable since the original receipt of the money is a sufficient con-

sideration for all promises, expressed or implied, with reference to its final disposition. *Walker* v. *Rostron*, 9 Mees. & W. 411; Mechem, Agency, §568." (Italics ours.)

Sayer v. *Wynkoop*, 248 N. Y. 54 (1928), is to the same effect. The Court said at page 59:

> "* * * the intention of the owner, and not that of the receiver, is controlling upon the question whether title to the moneys has been transferred and a trust has been created."

From a broader view of it, the relationship of the defendants to the whole subject was such as to bring about an implied trust.

In 2 Story's Equity Jurisprudence (12th Ed.) §1255, we read:

> "One of the most common cases in which a court of equity acts upon the ground of implied trusts in invitum, is where a party has received money which he cannot conscientiously withhold from another party. It has been well remarked that the receiving of money, which consistently with conscience cannot be retained, is in equity sufficient to raise a trust in favor of the party for whom, or on whose account it was received. This is the governing principle in all such cases, and, therefore, whenever any interest arises, the true question is, not whether money has been received by a party, of which he could not have compelled the payment, but whether he can now, with a safe conscience, *ex aequo et bono*, retain it."

Under these authorities the moneys received by the bankers upon the sale of the bonds and the notes were impressed with a trust enforceable by the corporation.

Since the moneys which Furlaud's banking house received from the subscribers to the bonds and notes were

held subject to a trust for the benefit of the corporation, it is difficult to see how anything which the promoters could contrive to have this *insolvent* corporation do could destroy its property rights as the beneficiary of this trust fund.

This was the basis of the District Court's decision.

POINT IV

THE PLAINTIFF IN HIS CAPACITY AS RECEIVER AND STANDING IN THE RIGHT OF THE CREDITORS HAS THE RIGHT TO DISAFFIRM THE ACTS OF THE CORPORATION.

Even if the defendants had succeeded in so committing the corporation to an approval of the fraudulent acts of the defendants as to disentitle the corporation itself to any remedy,—which we do not believe to be the case,—it is nevertheless entirely clear that the receiver, standing in the right of the creditors, could disaffirm the acts of the corporation.

The accepted doctrine is that a receiver may disaffirm acts of the corporation or its officers which were in fraud of creditors even though there might be a good defense to the suit as against the corporation itself.

In *Casey* v. *Cavaroc,* 96 U. S. 467, 488, 24 L. Ed. 779, 788 (1877), the Court said:

(At p. 488)

> "* * * The receiver does not represent the bank alone; he represents all the parties. He represents the law, which takes charge of the property for the benefit of all creditors, according to their respective and mutual rights. * * *

(p. 489-490)

> "Indeed, it may be laid down as a general rule, as well at the common law as the civil law, that a

> trustee, assignee or syndic, having the powers and occupying the relations which are sustained by a receiver under the National Banking Act, or an assignee in bankruptcy, may well oppose any privilege or preference which the law itself, unaided by a bona fide purchase or judgment, would regard as void against the general creditors in a direct contest between them and the parties claiming such privilege or preference; even though the debtor himself, on account of some personal disability arising from his own acts or engagements, could not resist the claim."

In *Leach* v. *Grant,* 54 Fed. (2d) 731 (C. C. A. 6th 1932), at page 733, the Court in discussing certain defenses which clearly would have been good if urged against the corporation as a party, said:

> "But this is not, as the argument assumes, a suit on behalf of the corporation for the rescission or partial rescission of an ultra vires contract; it is a suit on behalf of creditors and stockholders to recover for a fraud. The receiver, it is true, has not tendered back to appellant what the Struthers Company received in the transaction. He is not in position to do so, and in that situation the court will not require him to do the impossible thing of making a tender, but will take notice of all the circumstances, and, if equity and justice require, will permit a recovery on the implied obligation of the appellant to return the property which it has no right to retain, or, failing to do so, to make compensation therefor in money." (Citing *Davis* v. *Las Ovas Co.*)

Following these principles, the rule has become firmly established that the receiver stands in the rights of the creditors and may undo all corporate transactions which

were in fraud of the creditors' rights even though the corporation itself might not be able to do so.*

Nothing more need be said to demonstrate the grievous fraud which was practiced upon the innocent creditors of this corporation which these promoters through their fraudulent misappropriations rendered hopelessly insolvent at the start.

A stronger situation for applying the well established doctrine that a receiver may disaffirm acts of the corporation which are in fraud of creditors cannot well be imagined.

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*See: **Fed.**—*Atlantic Trust Co.* v. *Chapman*, 208 U. S. 360, 371, 28 S. Ct. 406, 52 L. Ed. 528; *Hamor v. Taylor-Rice Engineering Co.*, 84 Fed. 392, 399; *American Can Co.* v. *Erie Preserving Co.*, 171 Fed. 540, 542; *Graselli Chemical Co.* v. *Aetna Explosives Co.*, 252 Fed. 456, 460; *Westinghouse El. Mfg. Co.* v. *Binghamton Ry. Co.*, 255 Fed 378, 385. **Conn.**—*Greene* v. *Sprague Mfg. Co.*, 52 Conn. 330, 361. **Ill.**—*Peabody* v. *New England Water Works Co.*, 184 Ill. 625, 56 N. E. 951. **Ind.**—*Voorhees* v. *Indianapolis Car & Mfg. Co.*, 140 Ind. 220, 39 N. E. 738, 744. **Ky.**—*Industrial Mut. Deposit Co.'s Rec'r.* v. *Taylor*, 118 Ky. 851, 82 S. W. 574, 575. **Mass.**—*Williams* v. *Old Colony Trust Co.*, 222 Mass. 378, 110 N. E. 1029. **Minn.**—*German American F. Corp.* v. *Merchants & M. S. Bank*, 177 Minn. 529, 225 N. W. 891, 649 L. R. A. 582, 586. **Mo.**—*Alexander* v. *Relfe*, 74 Mo. 495, 516. **Nebr.**—*Williams* v. *Turner*, 63 Nebr. 575, 88 N. W. 668. **N. J.**—*Bradley* v. *United Wireless Tel. Co.*, 79 N. J. Eq. 458, 459, 81 Atl. 1107; Aff'd 83 N. J. Eq. 688, 93 Atl. 1084. **N. C.**—*Latta* v. *Catawba Elec. & Power Co.*, 146 N. C. 285, 59 S. E. 1028. **N. Y.**—*Pittsburgh Carbon Co.* v. *McMillin*, 119 N. Y. 46, 53; 23 N. E. 530. **Ohio**—*Smith* v. *Johnson*, 57 Oh. St. 486, 489; 49 N. E. 693, 694. **Penna.**—*Lyons* v. *Benney*, 230 Pa. 117, 119; 79 Atl. 250. **R. I.**—*Hayes* v. *Kenyon*, 7 R. I. 136, 141. **Utah**—*United States* v. *Church*, 5 Utah 538, 540; 18 Pac. 35. **Wash.**—*Wirkkala* v. *Wirkkala Bros. Logging Co.*, 109 Wash. 137, 186 Pac. 315, 316. **Wisc.**—*Harrigan* v. *Gilchrist*, 121 Wis. 127, 99 N. W. 909, 937.

See also 14a C. J. 990; 23 R. C. L. 116.

POINT V

THE CORPORATION WAS POWERLESS TO RENDER ITSELF INSOLVENT BY SURRENDERING TO THE DEFENDANTS ITS RIGHT TO HOLD THEM ACCOUNTABLE TO IT FOR THE PROCEEDS WHICH CAME INTO THE HANDS OF THE DEFENDANTS FROM THE ISSUANCE OF THE SECURITIES OF THE CORPORATION.

The officers and directors of the corporation with the assent of its stockholders may as a general rule commit the corporation, but when the rights of creditors are involved there are limitations upon the power of the corporation to act. *Fletcher Cyclopedia of Corporations, Permanent Edition;* Section 7407, states the rule in the following language:

> "As a general rule, an insolvent corporation cannot transfer its assets to the prejudice of creditors even though the action is joint by all the officers and stockholders" (See cases there cited).

The corporation was the creature of the defendants. They could commit it to much, but they could not commit it to everything. They went too far when they sought to commit it to an arrangement by which the proceeds from the securities which came into the hands of the defendants in a fiduciary capacity to the corporation and to its creditors were misappropriated by the defendants to such an extent as to render the corporation hopelessly insolvent.

POINT VI

IN THE HANDS OF THE DEFENDANTS ALL THE SECURITIES WERE VOID UNDER THE PENNSYLVANIA CONSTITUTION. THE DEFENDANTS AT NO TIME WERE IN THE POSITION OF STOCKHOLDERS, BONDHOLDERS OR NOTEHOLDERS OF THE CORPORATION.

It is alleged in the complaint and admitted in the answers that the Duquesne Gas Corporation is a corporation organized and existing under the laws of the State of Pennsylvania.

Article 16, §7 of the Constitution of Pennsylvania provides as follows:

> "* * * no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." Pennsylvania Act of April 17, 1876 (P. L. 30) §4 to the same effect.

The case of *Commonwealth* v. *Reading Traction Co.*, 204 Pa. 151, 53 A. 755 (1902), holds that the issuance of bonds or stock of a corporation for inadequate consideration is void, although the position of the innocent holders of the securities will be protected.

Both the Pennsylvania and Federal courts have applied this Constitutional provision to render invalid fictitious issues of stocks and bonds where they were not held by innocent purchasers. *Guarantee T. & T. Co.* v. *Dilworth Coal Co.*, 235 Pa. 594 (1912); *Bingaman* v. *Commonwealth Trust Co.*, 15 Fed. (2d) 119 (D. C. M. D. Pa. 1926); *In re Wyoming Valley Ice Co.*, 153 Fed. 787 (D. C. M. D. Pa. 1907), aff'd *sub nom. Weigand* v. *Albert Lewis Lumber & Mfg. Co.*, 158 Fed. 608 (C. C. A. 3rd 1908). Furthermore, it is not a case where the corporation alone is interested in declaring the transaction illegal. The fictitious

issuing of corporate securities is a question of public policy. *Gearhart* v. *Standard Steel Co.*, 223 Pa. 385 (1909).

The Supreme Court of Pennsylvania discussing the purpose of this prohibition has said:

> "The constitutional and statutory provisions referred to were designed to prevent unscrupulous persons from fraudulently issuing and placing on the market bonds or stock not fairly representing money or property received by the corporation." *Big Springs Electric Co.* v. *Kitzmiller*, 268 Pa. 34, 38 (1920).

Even if these bonds could have been said to have been in the hands of the promoters even for an instant, they would be void in *their* hands, under the Pennsylvania Constitution and decisions. Since the notes and stock were issued to the promoters without any consideration whatsoever, they were in their hands void under the Pennsylvania Constitution and decisions. It will not do to say that the 1,000 shares for which a payment of $500 was recorded are in any different position than the rest of the 675,000 shares. This $500 transaction was a part of the whole scheme which was for the immediate withdrawal by the promoters of not only this $500 but of about $1,500,000 besides of the corporate fund furnished by the bondholders and noteholders. The promoters were, therefore, not members of the corporation as valid stockholders or in any other sense at the time of the closing of the transaction.

Big Springs Electric Co. v. *Kitzmiller*, 268 Pa. 34 (1920) and *Bole* v. *Murray*, 233 Pa. 589 (1912) are authority for the proposition that the defendants are accountable under the Pennsylvania Constitution for the difference between the face amount of the bonds and notes and the consideration received by the corporation. The judgment granted by the District Court could have been sustained upon this ground alone.

POINT VII

THE DEFENDANT FURLAUD IS PERSONALLY ACCOUNTABLE FOR THE FRAUDULENT MISAPPROPRIATIONS.

The individual Maxime H. Furlaud and his associate Reuter were the promoters of the corporation. They personally planned and carried out the whole transaction. This is made clear from the beginning to the end of the record. There is not a word anywhere in the record to the contrary. The findings of the District Court are to that effect (R. 219, 220, 222, 229, 231).

They used their corporation called Furlaud & Company Inc. as well as the several dummy corporations, for the purpose of recording the voluminous corporate records which they created. After the fraud had been consummated, they caused the corporation Furlaud & Company Inc. to change its name to Winchelsea Holding Corporation and then caused it to be dissolved (R. 109). It is entirely manifest that these corporations acted wholly under their personal dominion.

In spite of this, the opinion of the Court of Appeals erroneously states at page 267:

> "Maxime H. Furlaud had no relation to these transactions other than as an officer and director of Furlaud & Company Inc., and his personal activity in carrying on the negotiations and transactions. He did not participate in the alleged fraudulent appraisal or receive personally any of the moneys paid to Furlaud & Company Inc."

While it is true that his associate promoter Reuter had more directly to do with the arrangement for the fraudulent appraisal, certainly there is no exculpation for Furlaud in that. The record clearly does not justify the

statement that Furlaud did not receive personally any of the moneys paid to Furlaud & Company, Inc. It is a fact that the record does not disclose the precise transactions by which these moneys came into the individual hands of Furlaud and Reuter, but the undisputed evidence shows that Furlaud and Reuter and their respective wives owned all of the stock of Furlaud & Company, Furlaud being the chief owner (R. 110, 111). The fact that soon after the consummation of their fraud Furlaud and Reuter caused their corporation to be dissolved compels the conclusion that the money received by their corporation came into their hands.

As demonstrated in Point I, these incorrect or misleading statements contained in the opinion of the Court of Appeals cannot disturb the effect of the findings of the Trial Court.

One may not cause a corporation which he dominates to commit a breach of trust without himself becoming accountable for the consequences. The dissolution of the corporation under the camouflaged name was manifestly for the purpose of hindering or defeating the rights of Duquesne Gas Corporation and of its creditors. This was Furlaud's final step in carrying out his breach of trust and in perpetrating the whole fraudulent scheme.

Anderson v. *Daley*, 38 App. Div. 505 (1899) (Appeal dismissed 159 N. Y. 146) is exactly in point. In that case one George A. Jones was an officer and director of Devlin & Company, a business corporation. One Daley (a bookkeeper of the company who was also a stockholder, officer and director of the corporation), was trustee under the will of Albert Ward, and as such deposited the moneys of the Ward estate with the corporation. Devlin & Company became insolvent, Jones died, and the beneficiaries of the Ward estate brought action to charge the estate of George

A. Jones with liability for the balance due the Ward estate by the corporation. The Court said (p. 512):

> "It does, however, clearly establish that Jones was aware of the insolvent condition of the corporation, and he also had knowledge that moneys of the estate were being furnished by the trustee and used in the business of the corporation. He was an active participant in the use of such moneys. * * * the evidence is clearly sufficient to charge him with knowledge and participation in their use for the business of the corporation, and, therefore, for his own benefit; and this is sufficient to charge him with liability * * *. *Nor can he shield himself by the fact that in what he did he acted as an officer of the corporation. The corporation could only act through its officers, and it is not essential that the misuse of the trust funds should be for the exclusive benefit of the person making such unlawful use, or indeed any benefit at all. Where he possesses the knowledge of the misuse of the trust funds, and knowingly applies them either for his own benefit or for the benefit of another, his liability is complete as the injury to the estate is the same whether he do it as an officer or as an individual. The basis of his liability is knowledge and injury, both of which here exist.*" (Italics ours.)

In any aspect of the case, there can be no question of the personal liability of the defendant Furlaud, for he, himself, planned and carried out the organization of the corporation and was himself a promoter, and as such, severally liable with his co-promoters for the secret profit which they obtained. *Bigelow* v. *Old Dominion Copper Mining & Smelting Co.*, 225 U. S. 111, 132 (1911).

Having appropriated shares of stock as a part of his secret profit he may be compelled to account for the $850,000 proved to have been received from the sale of a part of

it (*Chandler* v. *Bacon,* 30 Fed. 538, 540, and cases cited therein), as well as for the diverted trust fund which arose from the sale of the bonds and notes.

Defendant Kingston Corporation having participated in all the transactions is also liable for the whole amount diverted. The defendants Byron Corporation and Chaucer Corporation having each acted as the recipients of $425,000 from the proceeds of the sale of 85,000 shares of the stock of Duquesne Gas Corporation for the sum of $850,000 are each liable in the amount of $425,000.

POINT VIII

THE FORM OF THE DECREE.

The facts adduced at the trial were sufficient to permit of the framing of a final decree fixing the liability of the accounting defendants. The precise amount of net proceeds which came into the hands of the accountable defendants from the proceeds of the bonds, notes and stock was proved. The precise amount which the corporation received therefrom was proved. The figures are as follows:

Final net proceeds from $4,000,000 bond issue	$3,631,671.04
Final net proceeds from $1,000,000 note issue	861,097.69
Proceeds from the sale of 85,000 shares of stock	850,000.00
	$5,342,768.73

Cost of properties including the nine option properties and the several leases of undeveloped territory and including operating adjustments during the option period	$2,572,989	
Working capital	365,000	2,937,989.00
Amount received by the defendants from the bonds, notes and stock and diverted and misappropriated to their own use..		$2,404,779.73

The District Court properly held that the defendants as defaulting trustees were not entitled to be credited for services and disbursements in the course of defrauding the beneficiary. *Commonwealth Finance Corporation* v. *McHarg*, 282 Fed. 560 (C. C. A. 2d, 1922); *Davis* v. *Las Ovas Co.*, 227 U. S. 80 (1912); *Dunlap* v. *Twin City Power Co.*, 226 Fed. 161 (C. C. A. 4th 1915).

It was clearly to the interest of the receivership estate to avoid the expense and delay which would result from the making of an interlocutory decree for an accounting and the proceedings thereafter before a master. This would have entailed the reattendance of the numerous witnesses who reside at distant places, which, manifestly, would have led to long-drawn-out and expensive proceedings.

CONCLUSION

The judgment of the United States Circuit Court of Appeals for the Second Circuit, filed March 11, 1935, should be reversed and the decree of the United States District Court for the Southern District of New York

filed the 11th day of May, 1933, should be modified by increasing the amount of the judgment against the defendants Furlaud and Kingston Corporation by the sum of $850,000 with interest and by awarding judgment against the defendant Byron Corporation for $425,000 with interest and against the defendant Chaucer Corporation for $425,000 with interest and the decree of the District Court as so modified should be affirmed.

Respectfully submitted,

RALPH ROYALL
WILLIAM A. MAGEE
CLARK MILLER
Of Counsel.

September, 1935

APPENDIX

THE DECISION IN *OLD DOMINION COPPER MINING AND SMELTING COMPANY v. LEWISOHN*, 210 U. S. 206 (1908), AND THE OTHER DECISIONS OF THE FEDERAL AND STATE COURTS SINCE THAT TIME DEALING WITH THE SUBJECT.

The litigation growing out of the promotion of the Old Dominion Copper Mining and Smelting Company took a varied course. The corporation itself (there was no receivership) brought two suits which, except as to the defendants named, were substantially identical. One was the suit instituted in the Federal Court in New York against Lewisohn, one of the alleged fraudulent promoters, which resulted in the determination by the Supreme Court in 210 U. S. 206. The other was a suit brought in the State courts of Massachusetts against Bigelow, who was Lewisohn's associate as promoter. The Supreme Court of the United States held that the corporation had no right of action against its promoters to recover for a secret profit, since they owned all the stock of the corporation at the time of the transaction and were thus on both sides of the bargain, even though it was contemplated at the time that others should become stockholders by original subscription without knowledge of the secret profit. The Supreme Court of the State of Massachusetts (203 Mass. 159) reached the directly opposite conclusion. In a suit brought in New Jersey seeking to enjoin the corporation from pursuing Bigelow, the Supreme Court of New Jersey (74 N. J. Eq. 457) took the view of the Massachusetts court; and the United States Supreme Court itself in a later decision, *Bigelow* v. *Old Dominion Copper Company*, 225 U. S. 111, 56 L. Ed. 1009 (1912) refused to require the

Massachusetts court to conform to the Supreme Court's decision. Thus while one of the joint promoters of the Old Dominion Company escaped liability in the Federal courts, his fellow promoter was finally held liable by the Massachusetts courts.

These suits and the several phases of them in the United States, Massachusetts and New Jersey courts are reported as follows:

188 Mass. 315 (1905);
203 Mass. 159 (1909);
74 N. J. Equity 457 (1908);
136 Fed. 915 (1905);
148 Fed. 1020 (1906);
210 U. S. 206 (1908);
225 U. S. 111, 56 L. Ed. 1009 (1912);
195 Fed. 637 (1911);
202 Fed. 178 (1913).

The two latest decisions above referred to in the Federal courts involved a continuation of the same action after amendments to the complaint had been made. A brief history of the several suits and decisions growing out of the transaction is given by Judge Hough in 195 Fed. 637 (1911). Although Judge Noyes in the Circuit Court of Appeals (202 Fed. 178) indicated that he thought the amended complaint stated a cause of action in spite of the previous decision of the Supreme Court of the United States, recovery was denied on principles of estoppel and *res adjudicata*. (Writ of Cert. denied, 229 U. S. 613 (1913).)

The precise point of difference between the Supreme Court and the Massachusetts Court is, we believe, this: The Massachusetts Court adhered to a distinction, which

had been developed in earlier decisions that, if, at the time of the closing of the transaction, the promoters contemplated that there would at a later time be innocent subscribers to the stock of the corporation, the corporation could require the promoters to account for their secret profits; but that, if the promoters took all of the capital stock, although they contemplated reselling part of it to innocent purchasers, the contrary result would follow. The Supreme Court held that such a distinction depended too much upon form and was not acceptable. It held that the promoters were not accountable to the corporation unless at the time of closing the transaction there were innocent members of the corporation.

The Supreme Court, nevertheless, took pains to limit its decision to the particular facts of that case, for they say at page 216:

> "When, as here, after it (the corporation) really exists, it consents, we at least shall require stronger equities than are shown by this bill to allow it to renew its claim at a later date because its internal constitution has changed.
>
> "* * * if we should undertake to look through fiction to facts, it appears to us that substantial justice would not be accomplished, but rather a great injustice done, if the corporation were allowed to disregard its previous assent in order to charge a single member with the whole results of a transaction to which 13/15 of its stock were parties, for the benefit of the guilty, if there was guilt in anyone, and the innocent alike. We decide only what is necessary."

We do not believe there is a case in the books other than the decision now under review, where innocent and defrauded stockholders or bondholders furnished the money which was used to pay for the conveyance from

which the promoters derived their secret profit, in which the promoters have been able to obtain immunity on any theory. It does not matter what devices the promoters use or in what form they record the transaction. The above distinction which the Courts have made as to the form of the transaction does not under such circumstances apply. Cases to this effect are the well-considered cases of *California-Calaveras Mining Co.* v. *Walls,* 170 Cal. 285 (1915) and *Pittsburgh Mining Company* v. *Spooner,* 74 Wisc. 307 (1889).

The Supreme Court's *Lewisohn* decision, as the reasoning of the opinion clearly shows, has no application whatsoever to a situation in which, at the time of the closing, there were then others having a financial interest in the corporation who suffered from the promoter's secret profits. If there could otherwise be any doubt that the decision is thus limited, the matter is made perfectly clear by the decision in *Davis* v. *Las Ovas,* 227 U. S. 80 (1913). This case was decided at the same term as *Bigelow* v. *Old Dominion.* It is commented upon at pages 25-27 of the brief.

The Court in deciding *Davis* v. *Las Ovas* did not overrule the *Lewisohn* decision, but takes it as a case which was rightly decided on its own facts. But it may be noted that the Court held (227 U. S. 87) that "Neither is the corporate right of action defeated by the fact that the recovery will inure to the guilty as well as to the innocent, nor is the fact that all of the parties who may have shared in the secret profits are not sued fatal to the case;" also that the Court expressly approved the decisions in *Yeiser* v. *U. S. Board & Paper Co.* and *New Sombrero Phosphate Co.* v. *Erlanger,* which have generally been taken by the Courts in decisions both before and since the *Old Dominion*

cases as authority for a rule contrary to that of the *Lewisohn* decision.

In cases subsequently arising, the Federal courts generally have distinguished the *Lewisohn* case and applied the *Davis* v. *Las Ovas* case. The following are such cases:

In *Tilden* v. *Barber*, 268 Fed. 587 (D. C. N. J. 1920), the promoters were held liable to the corporation though they owned all the stock at the time of the transaction with the corporation. This result was reached on the theory that the promoters were in the position of trustees to subscribers who were to be future stockholders of the corporation. The court at page 598 quoted from *Yeiser* v. *U. S. Board & Paper Co.*

The Court of Appeals in the 6th Circuit again invoked this trust doctrine in *American Shipbuilding Co.* v. *Commonwealth S.S. Co.*, 215 Fed. 296 (C. C. A. 6th, 1914). It was there said that when the promoters commenced their negotiations for the organization of the company, they were acting as trustees for the future corporation and its stockholders.

The same result was reached in *Dunlap* v. *Twin City Power Co.*, 226 Fed. 161 (C. C. A. 4th, 1915).

In *Humble Oil Co.* v. *Campbell*, 69 Fed. (2d) 667 (C. C. A. 5th, 1934), which is the latest decision of the Federal courts upon the subject, the defendant issued and sold certificates of interest in certain oil properties owned by him and represented that all the proceeds would be turned over to the unit holders. In violation of the trust thus created the defendant sold a portion of the property and retained the proceeds. A corporation was organized to take over the property and the unit holders subsequently became shareholders in the corporation. In this suit by the receiver of the corporation it was contended that, under the doctrine of the *Lewisohn* case, no right of action existed

in favor of the receiver. But the court held that the defendant occupied a fiduciary relation to the unit holders and the future corporation, that where such a relationship exists the corporation may follow and gather in the trust property in spite of the rule of the *Lewisohn* case.

Such Federal cases as have applied the *Lewisohn* case in denying a recovery by the corporation, were, we believe, cases the decisions in which were ultimately based upon the fact that no fraud was actually practiced by the promoters. Those are the cases of *Ball* v. *Breed*, 294 Fed. 227, 231 (C. C. A. 2d, 1923); *South Penn Collieries Co.* v. *Sproul*, 52 Fed. (2d) 557, 561 (C. C. A. 3rd, 1931); *Johnson* v. *Louisville Trust Co.*, 293 Fed. 857, 861 (C. C. A. 6th, 1923).

The question involved in the *Old Dominion* cases has frequently arisen in the State Courts.

By 1905 a number of decisions had already set a strong precedent for holding the promoters fiduciaries and accountable to the corporation where the scheme contemplated the entry of innocent stockholders.

Fed.	*Yeiser* v. *U. S. Board & Paper Co.*, 107 Fed. 340 (C. C. A. 6th, 1901);
Mass.	*Hayward* v. *Leeson*, 176 Mass. 310 (1900);
Maine	*Land Company* v. *Lewis*, 101 Me. 78 (1905);
Penn.	*Bailey* v. *Pittsburgh etc. Co.*, 69 Pa. 334 (1871);
Wisc.	*Pittsburgh Mining Co.* v. *Spooner*, 74 Wisc. 307 (1889);
	Pietsch v. *Milbrath*, 123 Wisc. 647 (1905).

See also:

Fed.	*Chandler* v. *Bacon* (C. C. 1887), 30 Fed. 538;
	Cortes C. v. *Thannhauser* (C. C. 1891), 45 Fed. 730;

Cal. *Burbank* v. *Dennis*, 101 Cal. 90 (1894);
Ct. *Yale Gas Stove Co.* v. *Wilcox*, 64 Ct. 101 (1894);
Mo. *Land Co.* v. *Case*, 104 Mo. 572 (1891);
N. Y. *Brewster* v. *Hatch*, 122 N. Y. 349 (1890);
Penna. *Densmore Oil Company* v. *Densmore*, 64 Pa. 43 (1870);
Wisc. *Hebgen* v. *Koeffler*, 97 Wisc. 313 (1897).

Such has long been the rule in the English Courts:

New Sombrero Phosphate Co. v. *Erlanger*, L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rp. 436 (opinion of Jessel, *M.R.*) (1877);
Gluckstein v. *Barnes* (1900), App. Cas. 240 (opinion of Lord Macnaghten);
In re Leeds & Hanley Theatres, Ltd. (1902) L. R. C. D. 809.

Since the *Old Dominion* decisions the State Courts have often discussed the conflict between the Massachusetts decision in the *Bigelow* case and the United States Supreme Court decision in the *Lewisohn* case, and in that connection the *Davis* v. *Las Ovas* decision. In the following cases, the Courts have shown disagreement with *Old Dominion* v. *Lewisohn*.

Calif. *California Mining Co.* v. *Walls*, 170 Calif. 285 (1915);
Ken. *Datillo* v. *Roaten Creek Oil Co.*, 222 Ky. 378 (1927);
Mich. *Torrey* v. *Toledo Portland Cement Co.*, 158 Mich. 348 (1909);
American Forging Co. v. *Wiley*, 206 Mich. 664 (1919);
Neb. *Nebraska Mausoleum Co.* v. *Matters*, 108 Nebr. 618 (1922);

N. J. *Arnold* v. *Searing,* 78 N. J. Eq. 146 (1910); *Bigelow* v. *Old Dominion Copper Mining & Smelting Co.,* 74 N. J. Eq. 457 (1908);
N. C. *Goodman* v. *White,* 174 N. C. 399 (1917);
Ore. *Wills* v. *Nehalem Coal Co.,* 52 Ore. 70 (1908); *Rugger* v. *Mt. Hood Electric Co.,* 143 Ore. 193 (1933);
R. I. *Anderson* v. *Johnson,* 45 R. I. 17 (1923);
S. D. *Meier* v. *Eaton,* 46 S. D. 286 (1923).

See also:

Ariz. *Frame* v. *Mahoney,* 21 Ariz. 282 (1920);
Fla. *McNabb* v. *Tampa etc. Land Co.,* 78 Fla. 149 (1919); but *cf. Lake Mabel Development Co.* v. *Bird,* 99 Fla. 253 (1930);
Ga. *Downey* v. *Bird,* 171 Ga. 532 (1930);
Me. *Mason* v. *Carothers,* 105 Me. 392, 74 Atl. 1030 (1919);
N. J. *Allenhurst Park Estate* v. *Smith,* 101 N. J. Eq. 581, 138 Atl. 709 (1927).

And see note to *Davis* v. *Las Ovas* in 57 L. Ed. 426 and in 85 A. L. R. 1276-89; also *Ballantine Private Corporations* § 50.

Only a few of the states have indicated a preference for the *Lewisohn* decision.

See:

Colo. *Lilylands Canal Co.* v. *Wood,* 56 Colo. 130 (1913);
Minn. *Hoffman Motor Truck Co.* v. *Erickson,* 124 Minn. 279 (1914);
Wash. *Inland Nursery & Floral Co.* v. *Rice,* 57 Wash. 67 (1910);
W. Va. *Vasey* v. *Coal Co.,* 89 W. Va. 499 (1921).

But it may be pointed out that in those jurisdictions which have followed the rule of the *Lewisohn* case, the courts have recognized that, where the rights of creditors are involved, the result may be different. See particularly:

Hoffman Motor Truck Co. v. *Erickson*, 124 Minn. 279 (1914);

Inland Nursery & Floral Co. v. *Rice*, 57 Wash. 67 (1910);

Vasey v. *Coal Co.*, 89 W. Va. 499 (1921);

Johnson v. *Louisville Trust Co.*, 293 Fed. 857, 861 (C. C. A. 6th, 1923).

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Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of DUQUESNE GAS CORPORATION,

Petitioner,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

PETITIONER'S REPLY BRIEF

RALPH ROYALL,
WILLIAM A. MAGEE,
CLARK MILLER,
Of Counsel.

October, 1935.

Supreme Court of the United States

OCTOBER TERM, 1935
No. 26

GEORGE W. MCCANDLESS, as Receiver of DUQUESNE GAS CORPORATION,
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vs.

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

PETITIONER'S REPLY BRIEF

At page 2 respondents make a misleading statement. They say:

> "Kingston Corporation had at great expense acquired options on various properties upon which it had paid various sums of money (R. 51-52). These options were acquired in the latter part of 1929 and the early part of 1930."

In fact, the options when originally taken in the latter part of 1929 and in the early part of 1930 were mere gratuitous options (Pls. Exs. 2-10, R. 164-170). Later in anticipation of the general closing set for April 9, 1930 and so as to make the options enforceable, some comparatively small sums were paid to the optionors aggregating a total of $45,510 (R. 53-54, 170A). Pages 51 and 52 of the Record

which are referred to by the respondents show the purchase prices of the various properties. The above quoted statement of the respondents is phrased in such a way as to carry the suggestion that these large sums mentioned on pages 51 and 52 constitute the "great expense" of acquiring the options.

At pages 4 and 5 and again at pages 24-26, the respondents set out repetitiously a long quotation from the opinion of Judge Knox at pages 222 and 223 of the Record in an effort to make it appear that Judge Knox found that all of the securities of the Duquesne Gas Corporation belonged to the respondents at the time of the closing. We call the Court's attention to the fact that in each instance the respondents have deleted from this quotation the following which appears in Judge Knox's opinion at page 223:

> "Throughout the proceedings, representatives of the various security dealers who were to distribute the bonds to the public were waiting without the room in which the foregoing transactions were being consummated. They carried checks for the purchase price of the bonds which their firms had respectively undertaken to distribute. These checks totaled about $3,000,000 and they were immediately exchanged for about eighty percentum of the whole bond issue. When this had been accomplished, Furlaud & Company, Inc. out of the money so obtained, and with that which had come from Kingston Corporation, liquidated the credit which it had obtained from the Trust Company."

At page 6 of the Respondents' brief, the following appears:

> "The Court of Appeals recited the facts of the transaction between Duquesne Gas Corporation in

almost the identical language employed by the lower Court (R. 263-267). It then quoted the following from the opinion of the Trial Court: (R. 388-389)

> 'At the time that the transaction through which Duquesne Gas Corporation acquired the various gas properties were consummated, and for some time thereafter, Furlaud & Company, Inc. owned every share of its capital stock, and ratified and approved of the whole transaction.'

"Then follows the language complained of by the petitioner:

> 'At the end of these transactions, the two corporations, Furlaud & Company, Inc. and its subsidiary, Kingston Corporation, owned all of the issued common capital stock of the Duquesne Gas Corporation, and all of its bonds and notes. No other person purchased from Duquesne Gas Corporation a share of stock, a bond or a note' (R. 268).

"There is no question about the actual facts in this case.

"They are correctly stated by the Trial Court and by the Court of Appeals."

Read hastily in the foregoing context, the quotations from the opinions of the District Court and the Court of Appeals may seem much alike. *But they are vitally different.* The quoted part of the District Court's opinion is limited to the *capital stock,* while the opinion of the Circuit Court of Appeals goes further and says that the respondents "owned all of the issued common capital stock of the Duquesne Gas Corporation, *and all of its bonds and notes.*"

It is misleading to say that the two courts viewed the facts alike and used almost identical language. As shown by the above quoted part of Judge Knox's opinion which

the respondents deleted, the Trial Court's view of the facts was that a very large amount of bonds were paid for at the closing of the transaction between the promoters and the corporation by innocent bondholders and the bonds then issued to them, and that the moneys of these bondholders were used to pay for the properties upon which the promoters made their secret profit.

The respondents, themselves, virtually admit at pages 7-8 of their brief that a very large amount of the bonds were at the time of closing sold to various innocent purchasers and the proceeds used in payment for the property. At this point the most that they claim is that the amount thus received from innocent bondholders was only $1,886,330, or substantially less than the amount found by the Trial Court.

It is indisputable that these bonds were not issuable to anyone until the deeds to the corporation were delivered by the sellers and the mortgage securing the bonds recorded,—all of which occurred on April 9th, 1930 as a part of a simultaneous closing of the transaction between the promoters and the corporation, as a part of which closing the bank messengers from the various purchasers of the bonds made delivery of their certified checks against definitive delivery to them of the bonds. The statement, therefore, in the opinion of the Court of Appeals and in the respondents' brief that at the time of the closing of the transaction respondents "owned all of the issued common capital stock of the Duquesne Gas Corporation, *and all of its bonds and notes*" is a misstatement of a vital fact.

Respondents in Points I and II of their brief, pages 13-23, argue that the complaint is insufficient and that

there was a variance between the allegations and the proof, and, in this connection, that certain testimony was erroneously admitted. Their contention seems to come to this: that the complaint is to be viewed as an attempt to state a cause of action for misrepresentation and that it is insufficient, in that it does not allege that the misrepresentations were false or the other essentials of a cause of action for misrepresentation. This contention is reasserted at several other places throughout the brief. Respondents' effort to sustain the judgment of the Court of Appeals seems to be based chiefly upon this.

It is clear from the opinions below that both of the lower courts regarded the complaint as stating a good cause of action in equity for an accounting, and we submit that as to this the courts below were right.

The eighth paragraph of the complaint (R. 6-7) alleges the issuance of the bond and note circulars and refers to them in such a way as to show that a fiduciary relationship to the corporation arose from the statements in the circulars, making the defendants accountable to the corporation for the proceeds of the bonds and notes. The fiduciary relationship of the defendants to the corporation is also well alleged in the fourteenth paragraph (R. 9) as also arising from the fact that the defendants "Furlaud and Reuter were the promoters of said Duquesne Gas Corporation; that they caused it to be organized; that all the steps which were taken for the consummation of its incorporation, organization, issuance of its said bonds, notes and stocks were taken under the direction and at the behest of defendants Furlaud and Reuter; that they stand in a fiduciary relation to said Duquesne Gas Corporation; that defendants Furlaud and Reuter are accountable to the corporation for the proceeds derived from the issuance and sale by them as aforesaid of all of said securities of said

"corporation." The prayer for relief is full and in proper form as a prayer for relief for an accounting (R. 13).

The respondents merely treat the complaint as something of a nature entirely different from what it is in order to attempt to construct some argument in respect to it.

As to the contention respecting the admission of testimony, that is without the least merit. Their criticism along this line is rather general. The alleged errors are not clearly specified.

The bond and note circulars (prospectuses) and advertisements were put in evidence by the plaintiff (Pls. Exhs. 22, 23, 24, 25, R. 180-197). These prospectuses set forth a valuation of $7,039,000 for the corporate property, including working capital of $365,000. Plaintiff also proved that the cost of the property, excluding working capital, was $2,572,989 (R. 170A). The respondents do no seem to base their criticism upon the admission of the foregoing testimony.

The Trial Court brought out some evidence relating to the value of the property (R. 60) and the plaintiff proved facts showing the outrageous character of the respondents' steps in obtaining the fraudulent appraisal of part of the property, the facts as to which are sufficiently related at pages 219 and 220 of the opinion of the Trial Court. This seems to be what the respondents are now protesting about. As to the admission of evidence as to the value of the property, which the respondents seem to stress as the main error, it is entirely comprised of a statement of the witness Nuss in answer to questions by the Trial Court that his property was worth about what the corporation paid for it, viz.: $660,000, although it was included in the fraudulent appraisal at $2,500,000 (R. 16). Since the respondents were willing purchasers of the gas properties, which under their

scheme were to be paid for with other people's money, the selling price was presumably as much as the owners could get and all that the property was fairly worth. Whether the property was worth something more or less than it cost, the fact remains that these respondents, who stood in a fiduciary relation to the corporation, used it as a means of extracting the secret profit for which they should be held accountable. In any view of it, we submit that the facts relating to the proceedings of these fiduciaries in consummating their fraudulent scheme were manifestly relevant to the case and very material.

Respondents (pp. 31-38 of their brief) seem to agree that this Court's *Old Dominion* v. *Lewisohn* and *Davis* v. *Las Ovas* decisions, when read together, establish that it is enough to make promoters accountable to the corporation for a secret profit if other parties then interested in the corporation did not share in the profit and were without knowledge of it. They simply claim the fact to be that at the time of the closing of the transaction between the promoters and the corporation there was no one interested in the corporation excepting themselves. The plain fact of the matter is, however, that bondholders, without knowledge of the secret profit became interested parties at the moment of the closing and as a part of the closing transaction, and that their moneys were used to pay for the property out of which the secret profit was derived. Since the fraudulent misappropriations made by the respondents rendered the corporation insolvent at its start, the corporation and its creditors were grievously wronged. Upon such a state of facts and upon the respondents' own view of

the law, they are accountable to the plaintiff for the whole secret profit.

As Point IX of their brief, pages 55-57, respondents suggest that this Court fell into error in making its previous decision in this case, 79 L. Ed. 32. They neglect to call the Court's attention to the fact that they filed a petition for rehearing which was denied (79 L. Ed. 198). Respondents refer to this Court's decision in *Mitchell* v. *Maurer*, 79 L. Ed. 149. But it would seem that the respondents have not read very carefully *Mitchell* v. *Maurer*. This Court in the body of its opinion refers to its decision just then handed down in *McCandless* v. *Furlaud* and again refers to it in two separate footnotes. In one of the footnotes (numbered 4), the Court points out that:

> "The order appointing ancillary receivers attacked in *McCandless* v. *Furlaud* * * *, on the ground that the Court was without federal jurisdiction, had been entered, not in the suit there under review, but in a separate proceeding in the same court."

Another difference between the two cases is that, while in the instant case the primary receiver was appointed in the Federal Court, the primary receiver in the *Mitchell* v. *Maurer* case was appointed by a State Court.

CONCLUSION

The judgment of the United States Circuit Court of Appeals for the Second Circuit, filed March 11, 1935, should be reversed and the decree of the United States Dis-

trict Court for the Southern District of New York, filed the 11th day of May, 1933, should be modified by increasing the amount of the judgment against the defendants Furlaud and Kingston Corporation by the sum of $850,000 with interest and by awarding judgment against the defendant Byron Corporation for $425,000 with interest and against the defendant Chaucer Corporation for $425,000 with interest and the decree of the District Court as so modified should be affirmed.

Respectfully submitted,

RALPH ROYALL,
WILLIAM A. MAGEE,
CLARK MILLER,
Of Counsel.

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Supreme Court
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CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. [redacted]26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,

Petitioner (Plaintiff-Appellee-Appellant Below),

—against—

MAXIME H. FURLAUD and KINGSTON CORPORATION,

Defendants-Appellants-Appellees Below,

and

BYRON CORPORATION and CHAUCER CORPORATION,

Defendants-Appellees Below,

and

CARLOS REUTER,

Defendant Below.

BRIEF OF APPELLEES IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

LOUIS B. EPPSTEIN,
IRA W. HIRSHFIELD,
LOUIS J. ALTKRUG,
Of Counsel.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

No. .....

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,
Petitioner (Plaintiff-Appellee-Appellant Below),

—against—

MAXIME H. FURLAUD and KINGSTON CORPORATION,
Defendants-Appellants-Appellees Below,

and

BYRON CORPORATION and CHAUCER CORPORATION,
Defendants-Appellees Below,

and

CARLOS REUTER,
Defendant Below.

BRIEF OF APPELLEES IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

This brief is submitted in opposition to a petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit presented by the complainant herein.

The United States Circuit Court of Appeals for the Second Circuit reversed the decree entered by the United States District Court for the Southern District of New York in favor of complainant, upon the merits.

Statement.

I.

Concerning the Pleadings.

The amended complaint in this case, if it states a cause of action at all, does so upon the theory that as a result of certain representations made by Furlaud & Company, Inc. to the purchasers from it of securities acquired by it from the Duquesne Gas Corporation, it received the amounts paid to it for these securities by such purchasers as trustee for the Duquesne Gas Corporation.

The first seven paragraphs of the complaint are devoted to a description of the parties, their relations to one another and allegations affecting jurisdiction.

The eighth paragraph alleges the offerings of the securities and the representations made. Attention is called to the fact that the only allegation in the complaint as to representations made to purchasers was that it was stated: "These bonds were issued by the corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes," and in the case of the notes, "These notes are issued by the corporation in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes."

There is no allegation anywhere in the complaint that these statements were false nor that any person was deceived thereby nor that anyone was induced thereby to purchase any of these securities.

The ninth, tenth, eleventh, twelfth and thirteenth paragraphs contain allegations referring to the transaction between the parties.

The fourteenth paragraph alleges merely the conclusion that some of the defendants were promoters of the Duquesne Gas Corporation and that they stand in a fiduciary relationship to it.

The fifteenth and sixteenth paragraphs are devoted to the history of the transaction.

The seventeenth paragraph reads as follows:

> "That the complainant, as Receiver, is entitled on behalf of Duquesne Gas Corporation to have the defendants account to the corporation *for the funds or moneys coming into their hands or into the hands of any of them or their agents or representatives from the sale of the securities of said Duquesne Gas Corporation* or of any of said securities, and for the disposition made of such funds or moneys and to make restitution for any or all of such funds or moneys wrongfully diverted from Duquesne Gas Corporation and misappropriated or converted by the defendants or any of them to their own uses and for any or all secret or excessive profits taken or retained by them or any of them; that your complainant has no adequate remedy at law and your complainant's rights may only be properly adjudicated in this Court of Equity." (Italics ours).

We respectfully repeat here the position we have taken in the trial court and in the Circuit Court of Appeals namely, that this complaint does not state facts which constitute a cause of action in favor of Duquesne Gas Corporation or its receiver against any one.

II.

Concerning the Facts.

Petitioner contends that there is a conflict between the statement of facts as found by the Circuit Court of Appeals and that of the United States District Court, charging that in the opinion of the Circuit Court of Appeals at several places it states "that, at the time of the closing the defendants owned all of the issued common capital stock of the Duquesne Gas Corporation and all of its bonds and notes;" and that this was not true and that it was not so found to be true in the opinion of the District Court.

The trouble with this statement contained in the Petition for a Writ of Certiorari is that it is not in accord with the findings of fact of either court which, as we will show, are in accord upon this and every material subject.

The facts briefly are as follows:

Furlaud & Company, Inc., a corporation, owned all of the issued and outstanding stock of Kingston Corporation, a corporation organized under the laws of the State of New Jersey. It also organized and at the time of closing and for weeks thereafter owned all of the stock of Duquesne Gas Corporation. Kingston Corporation had acquired options on various properties upon which it had paid various sums of money and on April 7, 1930 these two wholly owned subsidiaries of Furlaud & Company, Inc. entered into an agreement of reorganization.

Quoting from Judge Knox's opinion (Record, p. 322, fols. 965-969):

"This instrument provided that Kingston

Corporation would acquire the optioned gas properties then in escrow, and turn them over to Duquesne Gas Corporation. The latter, on its part, agreed to pay $3,015,000. to Central Hanover Bank & Trust Company, the amount which Kingston Corporation would be under obligation to pay to the Trust Company. The Duquesne Company further agreed to issue 535,000 shares of its stock and $1,300,000. face value of its first mortgage six percent gold bonds to Kingston Corporation, the bonds to be secured by an indenture, dated March 15, 1930, in which the Trust Company was named as Trustee. On April 9, 1930, the following transactions were had at the offices of Central Hanover Bank & Trust Company:

"Maxime H. Furland arranged with the bank that for a period of one day the Kingston Corporation should have a credit of $3,015,000, and that Furlaud & Company, Inc. for a like period of time, should be entitled to a credit of $3,379,500.

"When these credits, which were both closely controlled by the Trust Company, had been set up, Kingston Corporation delivered its certified checks, in the aggregate amount of $2,449,900. to the Equitable Trust Company, Guaranty Trust Company of New York and Central Hanover Bank and Trust Company, respectively. These checks were intended to put the drawees in funds with which to meet drafts which had been drawn against them by the banks in Western Pennsylvania, which held in escrow the several instruments of conveyance by which the gas properties were to be transferred to Duquesne Gas Corporation * * *.

"The banking institutions which received the checks of Kingston Corporation having made

telephonic and telegraphic reports of the payments of the purchase money drafts to the banks holding the escrowed conveyances, the latter were straightway delivered and recorded. *This information, being received, Duquesne Gas Corporation proceeded to issue to Kingston Corporation the 535,000 shares of stock and $1,300,000 face value of bonds which were called for by the agreement of April 7, 1930.* (Italics ours).

"Thereupon, Furlaud & Company, Inc. delivered its check to Duquesne Gas Corporation in the sum of $3,379,500. This was supposed to represent the proceeds which the gas corporation was to receive for $2,700,000. par value of its six percent bonds, its million dollar issue of gold notes, and 139,000 shares of its capital stock. *All of these securities were contemporaneously delivered to Furlaud & Company, Inc.* * * *" (Italics ours).

These represented all of the securities ever issued by Duquesne Gas Corporation.

Quoting from Judge Manton's opinion (pp. 388-9 of the Record):

"As stated by the Court below:

'At the time that the transactions through which Duquesne Gas Corporation acquired the various gas properties were consummated, and for some time thereafter, Furlaud & Company, Inc., owned every share of its capital stock, and ratified and approved of the whole transaction.'

At the end of these transactions, the two corporations, Furlaud & Company, Inc. and its subsidiary, Kingston Corporation, owned all of the issued common capital stock of the Duquesne Gas

Corporation, and all of its bonds and notes. No other person purchased from Duquesne Gas Corporation a share of stock, a bond or a note."

From these quotations it will appear that there is no conflict between the findings upon this subject of the Circuit Court of Appeals and those of the Trial Court.

Moreover, there is no conflict in the testimony upon this subject.

Thomas W. Duke, who was counsel for Furlaud & Company, Inc. in charge of this transaction was put upon the stand by the Petitioner. His testimony, starting at page 117, of the Record, discloses the fact that the money used in paying for the properties was furnished by Furlaud & Company, Inc., that the transaction was concluded exactly as stated in the opinion of Judge Knox and summarized in the statement of Judge Manton—that after the purchase price of the properties had been paid by Kingston Corporation, the deed and mortgages recorded and the securities duly authenticated, the stock and securities were all released to Kingston Corporation and Furlaud & Company, Inc. respectively.

What, then, is the position of the Petitioner in this case?

As stated by both courts in effect, the receiver has always contended and still contends that misrepresentations, as to the value of the property acquired by Duquesne Gas Corporation in this transaction, *made by Furlaud & Company, Inc. to purchasers from it on the resale of the securities so acquired,* constituted a wrong to Duquesne Gas Corporation for which the receiver of that corporation may now recover. He contends that as the result of such alleged misrepresentation the purchasers were induced to part with their money and that as a further

result a trust in this money arose in favor of Duquesne Gas Corporation.

The receiver further contends that even though any cause of action arising out of such alleged misrepresentation was personal to the party deceived thereby to his harm, and even though said party had the right of election of various remedies, this receiver in his official capacity was empowered to vindicate the rights of creditors who were victimized. Opinion by Knox, *D. J.*, Record, pages 332-333, folios 996-997.

We have never contended that if in the sale or resale of securities material misrepresentations were made to a purchaser who in reliance upon such representations made such purchase, that a cause of action would not result in favor of the purchaser so deceived.

What we do contend is that as a result of such transaction, no trust would be created in favor of the corporation that issued such securities.

In the opinion by Knox, *D. J.*, the theory upon which this case was tried in the lower court is presented as follows (fols. 952-953, p. 318 of the Record):

> "This is a suit in equity brought by complainant, as Receiver of Duquesne Gas Corporation, to compel defendants to account
>
> 'for all funds or moneys coming into the hands of them or any of them, or of the agents or representatives of any of them, or in the hands of anyone else acting with or for them, *from the sale* of the bonds, notes and shares of stock of said Duquesne Gas Corporation.'
>
> "The special grievance of the bill is that defendants, or some of them, through the instrumentality of an alleged banking house, known as Furlaud & Co. Inc., came into possession of

funds arising from the public offerings of securities of Duquesne Gas Corporation, in the relationship of fiduciaries to that company, and that a large portion of the funds so received, were diverted and misappropriated from the treasury of the gas corporation." (Italics ours.)

An examination of the complaint will show that the complaint contained no allegation charging misrepresentation of any kind.

As we have shown the only representation referred to in the complaint was the representation as to the purposes of the issue. As to that there is no allegation in the complaint that it was not true. Moreover, that representation, as shown by the evidence, was literally true. There is nothing in the complaint showing that any representations were made to the public as to the value of the property acquired by Duquesne Gas Corporation, nor is there anything in the complaint alleging what the value of the property transferred to Duquesne Gas Corporation was.

Upon the trial of the case, however, evidence was introduced tending to establish the fact that the notices issued upon the public offering of these securities contained statements to the effect that appraisals had been made of the property by engineers fixing the value, including working capital, at $7,038,000 and that at least one of these appraisals greatly overestimated the value of the property included in it.

This evidence was admitted over the most strenuous objection of the defendants who insisted that it was not admissible under the allegation of the complaint, claimed surprise and stated that they were not prepared to proceed upon that issue. They objected so persistently that finally a stipulation was made in open court that defendants should be con-

sidered to have a blanket exception to the admission of all testimony upon this subject (Record, fols. 250-269, 270-280, 290-299, 461-465, 480-484).

Upon the appeal to the Circuit Court of Appeals, the defendants, among other things, asked for the reversal of this case upon the ground that such evidence was improperly admitted and considered by the Court.

Attention is here called to this testimony because it became the basis for the entire attack upon the transaction and it was upon this testimony that the District Judge justified his decision.

Argument.

In his petition for a writ, Petitioner presents his propositions under the headings of "The Questions Presented".

Questions (1) and (2)

Under the first and second questions so presented, Petitioner asks whether the case falls under the authority of *Old Dominion Copper Company* v. *Lewisohn,* 210 U. S. 206 (52 L. Ed. 1025), rather than within the authority of *Davis* v. *Las Ovas,* 227 U. S. 80 (57 L. Ed. 426).

We again respectfully call attention to the fact that under the pleadings in this case, if complainant can recover at all it must be upon the theory that a misrepresentation made by a banker in the resale of securities purchased by him, impresses upon the money received by him, from such sale, a trust in favor of the corporation which issued the securities.

This suit is not brought to recover alleged secret profits but the complaint demands an accounting of certain sums of money which it contends became a trust fund.

However, answering the questions categorically and assuming for the sake of the argument that the complaint was drawn in such manner as to make the inquiry pertinent, we call attention to the facts:

In the case of *Davis* v. *Las Ovas, supra,* there were innocent stockholders involved at the very time of the transaction complained of.

In the transaction between Duquesne Gas Corporation and its promoters there were no other parties involved. The promoters and the promoters alone were on both sides of the transaction. They transferred to Duquesne Gas Corporation, their wholly owned subsidiary, certain property and money and received in return every share of stock and every security ever issued by Duquesne Gas Corporation. No other person ever dealt with that corporation for any of its securities.

If the promoters had retained all of these securities, the question could not have arisen.

If the promoters had disposed of the securities to strangers with full notice of all of the facts, the question could not have arisen.

If then, in the resale of these securities it be admitted for the sake of the argument, that misrepresentations as to the value of the property conveyed to the Duquesne Gas Corporation were actually made, would that *nunc pro tunc* create a cause of action in favor of Duquesne Gas Corporation?

We think the language of this Court in the case of *Old Dominion Copper Company* v. *Lewisohn, supra,*

upon this subject disposes of this question. Mr. Justice Holmes, speaking for this Court, said:

> "If there was a wrong, it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation *nunc pro tunc,* but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. For it is only by virtue of the innocent subscribers' position and the promoter's invitation that the corporation has any pretense for a standing in court. If the promoters, after starting their scheme, had sold their stock before any subscriptions were taken, and then the purchasers of their stock, with notice, had invited the public to come in, and it did, we do not see how the company could maintain this suit. If it could not then, we do not see how it can now."

Petitioner attempts to distinguish the rule announced in the case of *Old Dominion Copper Company* v. *Lewisohn,* 210 U. S. 206, 52 L. Ed. 1025, as applied in *Ball* v. *Breed,* 294 Fed. 227, from the facts of this case upon various grounds.

Petitioner seems to have forgotten that in the application to this Court for a writ of certiorari in *Ball* v. *Breed,* practically the identical questions were presented as are presented in this petition and that the writ was refused.

Further, on page 15 of the Petition, Petitioner says with reference to the case of *Ball* v. *Breed, supra,* and others:

> "* * * the decisions seem to be based more upon the fact that in those cases, the promoters' profits were not excessive or secret."

In the case of *Ball* v. *Breed,* the profits amounted to $1,100,000. In this case if the expenses incurred by the promoters in procuring the property had been allowed and the securities received had been given the same value as the corporation received for other securities, the profit would have amounted to $1,170,000.

In the case of *Ball* v. *Breed,* not only was a syndicate to purchase and distribute formed, but a twenty per cent. call was made upon the syndicate and paid in in *advance* of the closing transactions between the Bankers and the H. A. Co., and the money produced as a result of this call came into the hands of the promoters as managers of the syndicate and was the identical money used in purchasing the first block of H. A. Co. stock.

It is true that in this case, the bankers had negotiated for the sale of some of the securities which they were to acquire from the Duquesne Gas Corporation prior to the date of closing but they were unable to lay their hands on the money and did not get possession of any of the money which was to be paid them in exchange for those securities in advance of the closing but only after the securities had actually been issued and delivered to them. It was, therefore, necessary for them to furnish the funds with which to acquire the property to close the transaction out of their own resources before they could acquire the securities to resell to the prospective purchasers. In order to accomplish this, the Petitioner himself has shown that they caused two day loans to be made by the Central Hanover Bank & Trust Company, one for $3,015,000 to the Kingston Corpo-

ration and the other for $3,379,500 to Furland & Company, Inc. (fols. 349 and 355, pp. 117 and 119 of the Transcript of Record) and that they independently borrowed from Chatham & Phenix National Bank & Trust Company $700,000, from Hibernia Trust Company $300,000, and from the Pacific Trust Company $500,000 (fols. 378 and 379, pp. 126-127 of the Transcript of Record). With this money they paid for the property under option and closed the transaction with Duquesne Gas Corporation and after receiving the securities proceeded as rapidly as they could to sell same and pay off the day loans. Some were distributed upon the very day of the closing in consummation of contracts previously made. The amount received from these, as shown by Mr. Halporn who made the calculation in open court from the books of the corporation at the request of the Court, is fixed at $1,886,330 (fol. 542, p. 181 of the Transcript of Record). Based upon the estimate of a salesman, who was not present at the closing and did not pretend to know exactly what amount was actually delivered on that day, that about 75 to 80 per cent. had been subscribed for at some time or other, the Trial Court found another amount.

We do not think that this question is at all material. Obviously, if the fact that prior to the closing the bankers entered into contracts for the sale of the securities that they intended to acquire, if as and when they acquired such securities, had the effect of making the purchasers of such securities innocent members of the corporation, it is apparent that a sufficient number of people indicated their willingness to buy these securities if issued and, after they were issued, actually did buy them to make the exact amount of such purchases immaterial.

Petitioner contends that the dealings of Furlaud & Company, Inc. with its distributing group prior to the closing had the effect of bringing this within the rule of *Davis* v. *Las Ovas, supra.* However, in that case the corporation was actually organized by the syndicate itself (the defendants being members of that syndicate) and the original issue of the stock of the corporation was subscribed for and delivered by the corporation simultaneously to the other members of that syndicate as well as to the promoter member of the syndicate who made the secret profit complained of in that case.

The case of *Davis* v. *Las Ovas* was fully considered by the Circuit Court of Appeals of the Second Department in its decision in the case of *Ball* v. *Breed, supra,* and this very distinction was pointed out. The Court said (p. 232):

> "In *Davis* v. *Las Ovas,* 227 U. S. 80, 33 Sup. Ct. 197, 57 L. Ed. 426, the court held that, where the true consideration of a syndicate purchase is concealed, and the property is conveyed at a higher figure in shares of stock to a corporation *whose stock is held partly by members of the syndicate and partly by others,* and the necessary increase of shares to pay for the property goes to some of the syndicate promoters as a secret profit, the corporation may maintain an action to require those obtaining the shares to surrender them for cancellation." (Italics ours.)

Continuing, this Court says (p. 232):

> *"In the case at bar, there is no such state of facts. It is nowhere alleged as a fact, nor can it be inferred, that there were any innocent stockholders at the time of the transaction complained of. If, then, there was a fraud, it was not against*

the corporation, and a cause of action, if any, is personal to the purchasers of the stock. The fraud, if any, is what has been called a subsidiary fraud not affecting the corporation. Allowing to the complaint the most favorable inference, all that can be said is, as concisely stated by the District Court, that:

> 'These transactions between the defendants and the subscribers to their syndicate had nothing to do with the formation of the corporation, the syndicate subscribers only agreed with the syndicate managers to take what the managers get for them, and they got it through the managers.'" (Italics ours.)

In this case the transactions between Furlaud & Company, Inc. and the members of its syndicate, and the transaction between the syndicate and the distributing group, had nothing to do with the formation of the corporation. The syndicate subscribers and the distributing group only agreed with the syndicate managers to take what the managers got for them and they got it through the managers. The syndicate in the *Las Ovas* case was composed of co-adventurers, a partnership so to speak. The syndicate here were buyers from Furlaud & Company, Inc.

Moreover, we again call attention to the fact that even if the facts in this case fell within the doctrine laid down in the case of *Davis* v. *Las Ovas,* this complainant could not recover in this case upon that theory upon the complaint here.

The complaint does not allege any facts under which a recovery could be had upon that theory. There are no allegations of facts under which such relief was or could be asked for. The complaint proceeds upon the theory that the promoters received certain

sums of money from the purchasers of these securities under such circumstances that a trust was impressed upon the monies received by them, and the complaint demands that they be compelled to account for the proceeds of the sale of these securities. The complaint does not allege that there were any innocent members of the corporation at the time of the closing but is based solely upon the proposition that because of certain representations made to prospective purchasers of securities to be acquired by Furlaud & Company, Inc., a duty arose upon the defendants or some of them to account to Duquesne Gas Corporation for the proceeds of the sale of these securities.

On page 4 of his brief in support of petition the position of the Petitioner is stated very clearly:

> "The bondholders and noteholders must have intended that the proceeds of their subscriptions were to be used for the benefit of the corporation. The defendant well knew this, for the simple reason that the prospectuses which they issued induced in the subscribers to the bonds and notes this belief.
>
> "Where one delivers money to another with the intention that that other shall pay the money to a third person, a trust arises which may be enforced by that third person. *McKee* v. *Lamon,* 159 U. S. 317, 322; *Sayer* v. *Wynkoop,* 248 N. Y. 54; 2 Story's Equity Juris. (12th Ed.), Sec. 1255; 26 R. C. L. 1235, Sec. 82."

We do not believe that the foregoing statement correctly announces the proposition of law asserted in the cases cited, but a complete answer to this contention of Petitioner is that no one delivered money to Furlaud & Company, Inc., with instructions to, or

with the intention that Furlaud & Company, Inc. should pay the money to Duquesne Gas Corporation.

There is not a word of testimony to that effect.

The real transaction between Furlaud & Company, Inc. and the purchasers of these securities was that Furlaud & Company, Inc. offered the securities for sale if, as and when issued, the purchasers bought the securities and after they were issued received the securities from Furlaud & Co. Inc. and paid for them, and so far as the record in this case shows no purchaser of such securities was aggrieved by anything that Furlaud & Company, Inc. did. The complaint does not allege that any misrepresentations were made, it does not appear that any one was deceived by any representation made or was thereby induced to purchase a single security, nor does it appear from the complaint that any purchaser was dissatisfied with his purchase or that he was not recompensed by Furlaud & Company, Inc. for any loss sustained by him. Upon all of these questions which would be very material in a suit brought by one of these purchasers not only the complaint but the testimony is wholly silent.

No principle of equity jurisprudence is more firmly fixed than that the *allegata* and *probata* must correspond and that, the plaintiff, in equity, cannot recover if his proof does not harmonize with the allegations in his bill. Any other rule would do away with the necessity of pleadings and lead to surprise, unfairness and injustice. From the earliest time this principle has been announced and reannounced by this Court.

In the case of *Foster* v. *Goddard,* 1 Black 506, the Supreme Court of the United States, per Mr. Justice Swayne, said (p. 518):

"In equity proceedings the proofs and allega-

tions must agree. A party can no more succeed upon a case proved, but not alleged, than upon a case alleged, but not proved. *Simms* v. *Guthrie,* 9 Cranch 19; *Harrison* v. *Nixon,* 9 Pet. 483; *Boone* v. *Chiles,* 10 Pet. 178; *Trip* v. *Vincent,* 3 Barb. C. H. 613; *Bank of U. S.* v. *Shultz,* 3 Ohio R. 61; *Sadler* v. *Glover,* 5 Dana, 552; *Breckenridge* v. *Ormsby,* 1 J. J. Marsh 236."

In *Harrison* v. *Nixon,* 9 Pet. 483, Mr. Justice Story stated (p. 503):

"Every bill must contain in itself sufficient matters of fact, *per se,* to maintain the case of the plaintiff; so that the same may be put in issue by the answer, and established by the proofs. The proofs must be according to the allegations of the parties; and if the proofs go to matters not within the allegations, the court cannot judicially act upon them as a ground for its decision; for the pleadings do not put them in contestation. The *allegata* and *probata* must reciprocally meet and conform to each other."

In the case of *Crocket* v. *Lee,* 7 Wheat. 522, Mr. Chief Justice Marshall, in discussing a similar situation, said (p. 526):

"The counsel for the appellant says it would be monstrous, if, after the parties have gone to trial on the validity of the entry, and have directed all their testimony in the Circuit Court to that point, their rights should be made to depend in the appellate court on a mere defect in the pleadings, which had entirely escaped their observation in the Court where it might have been amended, and the non-existence of which would not have varied the case.

"The hardships of a particular case would not justify this tribunal in prostrating the fundamental rules of a court of Chancery—rules which have been established for ages, on the soundest and clearest principles of general utility. If the pleadings in the cause were to give no notice to the parties or to the Court of the material facts on which the right asserted was to depend, no notice of the points to which the testimony was to be directed, and to which it was to be limited; if a new case might be made out in proof, different from that stated in the pleadings, all will perceive the confusion and uncertainty which would attend legal proceedings, and the injustice which must frequently take place. The rule that the decree must conform to the allegations, as well as to the proofs of the parties, is not only one which justice required, but one which necessity imposes on Courts."

This doctrine has been reaffirmed by this Court as recently as in the case of *Garrett* v. *Louisville & N. R. Co.*, 235 U. S. 308.

Moreover, in this case the vice of the Petitioner in completely abandoning the allegations of fact and the theory advanced in his complaint and amended complaint is magnified by the following circumstance.

When this amended complaint was served upon the defendants they were at a loss, as they still are, to understand upon what theory the plaintiff could recover.

Prior to answering the amended complaint, the defendants made an application, pursuant to Equity Rule 20, to compel the complainant to make a further and better statement of the nature of the claim set forth in the amended complaint (fols. 55-99).

This application was opposed by counsel for the complainant on the ground that the complaint complied with Equity Rule 25. Counsel stated in his affidavit that the action was brought to compel fiduciaries to account to:

> "* * * Duquesne Gas Corporation and to complainant as its Receiver for all funds or monies coming into the hands of them or any of them from the sale of the bonds, notes and shares of stock of Duquesne Gas Corporation" (fol. 109).

The plaintiff here had the fullest opportunity to re-state his case and to allege all of the facts upon which he intended to rely. He had not then alleged and has never since alleged any facts showing or tending to show the concealment of any fact by any party. True, he alleges that certain representations were made, which representations taken alone were admittedly true.

Complainant does not even suggest that they were not true, nor does he allege any fact which taken in connection with such allegations would taint them with the charge of being made with the intent to deceive.

It is true that upon the trial he introduced evidence over the strenuous objection of the defendants to the effect that certain other representations, nowhere pleaded, were made to the purchasers of these securities and that such representations were in fact not true.

We have shown that even these so-called misrepresentations would not entitle the complainant to recover even though they might have created a cause of action in favor of some one else.

What we are calling attention to is the fact that the amended complaint in this case fails to contain any

allegations of misrepresentation and the further fact that complainant as a result of defendants' motion had the fullest opportunity to file a proper complaint and to make a further and better statement of the nature of the claim upon which he intended to rely and that he failed and refused to do so.

Questions (3) and (5)

The third question asked by the Petitioner will be treated with the fifth.

The two questions amount to this: "Would the fact that the corporation was rendered insolvent as a result of the transactions with its promoters, give to the receiver, acting in the interest of the purchasers of the securities, the right to disaffirm the acts of the corporation?"

There is no allegation in the complaint showing or tending to show that the corporation was insolvent at the time of its organization, and we therefore insist that the inquiry here presented for the first time, is in no wise pertinent.

Nor has petitioner ever sought to disaffirm the acts of the corporation. He is and always has been asking for an accounting of the proceeds of the resale of securities upon which he insists a trust was impressed as the result of certain representations made at the sale thereof.

Again, however, assuming for the purpose of the argument only, that the issue was presented, we insist that no cause of action growing out of those facts would have accrued to Duquesne Gas Corporation, or to its Receiver.

At the time of the transaction between the promoters and Duquesne Gas Corporation, no wrong was done to any one. The promoters transferred to their

wholly owned subsidiary certain property receiving in exchange for it all of the securities ever issued by such wholly owned subsidiary.

Obviously no wrong to Duquesne Gas Corporation resulted from this transaction.

If they had retained these securities, no wrong could have resulted to any one.

If they had disposed of all their securities with full disclosures of all of the facts no wrong could have resulted to any one.

If they had disposed of their securities under such circumstances as would have resulted in a fraud upon the purchasers thereof, the position of Duquesne Gas Corporation would have remained the same as before but, the purchasers might in that event have been injured and if so, each purchaser harmed would have had a cause of action against the sellers. However, such cause of action would have been personal to the party aggrieved.

Question (4)

The fourth question presented is not fairly within the issues. There is nothing in the notice which could be construed to be a statement or promise that the proceeds of the sale of the securities sold by Furlaud & Company, Inc., were to be used for any particular purpose. The transactions between Furlaud & Company, Inc. and the persons to whom it sold securities were ordinary transactions of sale. Furlaud & Company, Inc. had categorically stated that it had bought these securities "if as and when issued and approved by its counsel" and was offering them to a selected group of distributors (Record, p. 255, fol. 764).

The representation complained of simply stated that under the caption "Purposes of the Issue" Fur-

laud & Company, Inc. had stated that the securities were issued in connection with the acquisition of property and to provide working capital for the corporation.

However, for the purpose of this discussion only, let us assume that the representations were as stated by Petitioner, and that they were false and that the purchasers of these securities were deceived thereby. How could any representation made by Furlaud & Company, Inc. in the resale of these securities injure Duquesne Gas Corporation? It, Duquesne Gas Corporation, with full knowledge of all of the facts had concluded its transaction. At that time it admittedly had no cause of complaint against any one.

Certainly, misrepresentation made by Furlaud & Company, Inc. in the resale of the securities might create an actionable wrong but the injury resulting from such misrepresentation would not be to Duquesne Gas Corporation but to the purchasers of the securities, and any cause of action resulting therefrom would be theirs.

Question (6)

As to the individual liability of the defendant Maxime H. Furlaud—the record shows that all of the transactions in connection with the acquisition of the property were conducted by others, and Furlaud is not shown to have had anything to do with any of these transactions. However, he was the President of Furlaud & Company, Inc. and did negotiate and secure from various banks the funds required to close the transactions. If the money received by Furlaud & Company, Inc. in payment for the bonds sold by it to various purchasers was impressed with a trust in favor of Duquesne Gas Corporation, it may be

that Furlaud individually as an officer of that corporation might become obligated to see that the trust was executed and if the funds were diverted with his knowledge and consent it might be that he would be liable as a trustee *de son tort.*

Is it not, however, too clear for argument that the transaction engaged in by Furlaud & Company, Inc. in selling these securities was merely an ordinary transaction involving the sale of its property. It delivered the property sold and received the purchase price. It is not here contended that but for the alleged representations made in the resale of these securities any one could have complained.

We insist that the only persons who could have been injured by such representations, would have been the persons to whom they were made and that any causes of action that might result therefrom would be the causes of action of such persons.

There is in this case no allegation or proof that any person was misled by any representations made in these circulars, nor that any one acted on them, or complained because of them.

Recapitulation.

We contend:

1. That the complaint in this case does not state a cause of action in favor of any one, or against any one, upon any theory:

A. Because it nowhere alleges that the representations made as to the purposes of the issue or upon any other subject were false;

B. Because it nowhere alleges that the property conveyed to Duquesne Gas Corporation was not fully worth the amount paid for it;

C. Because it nowhere alleges that there was any representation of overvaluation or other misrepresentation made to the purchasers of the securities or to any one else.

D. This complaint does not even allege facts sufficient to establish a cause of action in favor of a purchaser of these securities.

It nowhere alleges that any representations made by the sellers were false nor that any one was deceived thereby or was induced thereby to purchase any of the securities so offered.

The complaint proceeds wholly upon the theory that where a banking house of issue makes representations, to purchasers of its securities from it, that the securities were issued in connection with the acquisition of property and to provide cash for development, extension and other corporate purposes, that such representations whether true or false, impress a trust upon the proceeds of the sale of such securities in favor of the corporation that issued the securities.

We do not think it requires the citation of authorities to negative this proposition.

2. That even including the evidence improperly admitted in this case, the facts disclosed would not under any theory establish a cause of action in favor of Duquesne Gas Corporation or its receiver because:

A. At the conclusion of the transactions between the Duquesne Gas Corporation and its promoters and as a result thereof they, the promoters, acquired all of the stock, all of the bonds, and all of the notes ever issued by that corporation and at that time were the sole owners of the corporation and were its sole creditors.

B. Even if in the resale of these securities these promoters made misrepresentations as to the value of the property owned by Duquesne Gas Corporation and the purchasers of such securities or any of them were injured thereby, such acts on their part could not create a cause of action in favor of Duquesne Gas Corporation.

If a cause of action in favor of various purchasers of securities did result from any transaction between such purchasers and any of these defendants, neither Duquesne Gas Corporation nor its receiver had any title to or interest in such cause of action. Whatever rights accrued to any of such purchasers would depend upon the particular circumstances of the transaction between each purchaser and his vendor.

Moreover, the owner of that cause of action would have an election of remedies. He might rescind, if he so elected. He might bring an action at law for the wrongs, if any, done him, but as has so often been said by the authorities not only would such cause of action be personal to the party aggrieved but the right of election would be his and his alone.

We respectfully submit that whatever may be the rights of others against the promoters of Duquesne Gas Corporation, the complaint in this case does not allege nor does the evidence, including that improperly admitted, establish any cause of action on behalf of Duquesne Gas Corporation against them.

We therefore respectfully pray that the petition for a writ of certiorari be denied.

Respectfully submitted,

LOUIS B. EPPSTEIN,
IRA W. HIRSHFIELD,
LOUIS J. ALTKRUG,
Of Counsel.

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Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,

Petitioner,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION and CHAUCER CORPORATION

LOUIS B. EPPSTEIN,
IRA W. HIRSHFIELD,
LOUIS J. ALTKRUG,
Of Counsel.

October, 1935.

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Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,
Petitioner,

vs.

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, *et al.*

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR RESPONDENTS MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION and CHAUCER CORPORATION

This case comes before this Court on writ of certiorari granted to the United States Circuit Court of Appeals for the Second Circuit on the 13th day of May, 1935 (R. 275).

The petitioner in his brief has outlined the previous proceedings and has referred to the previous opinion of this Court and the opinions below.

STATEMENT OF THE FACTS

Petitioner contends that there is a vital conflict between the findings of fact by the Trial Court and by the Court

of Appeals. We respectfully insist that this is not true. On page 17 of his brief, petitioner says:

> "The Appellate Court, although stating the facts quite differently from the finding of the Trial Court, nevertheless made no attempt to demonstrate that any finding was erroneous."

Later, on the same page, petitioner says:

> "The error of the Court of Appeals arises chiefly from its misstating a vital fact, viz: that at the time of the closing the defendants 'owned all of the issued Common capital stock of the Duquesne Gas Corporation and all of its bonds and notes' "

We insist that there is no material difference between the facts upon this subject as found by the District Court and by the Court of Appeals.

The undisputed facts are as follows:

Maxime H. Furlaud and Carlos Reuter owned all of the common stock of Furlaud & Company, Inc., a New York corporation (R. 110).

Kingston Corporation, a New Jersey corporation, was a wholly owned subsidiary of Furlaud & Company, Inc. (R. 219).

Kingston Corporation had at great expense acquired options on various properties upon which it had paid various sums of money (R. 51-52). These options were acquired in the latter part of 1929 and the early part of 1930. On February 21, 1930, the Duquesne Gas Corporation which was also a wholly owned subsidiary of Furlaud & Company, Inc. was organized. This corporation originally had an authorized capital structure of one thousand (1,000) shares of no par common stock (R. 220).

In March, 1930, the Duquesne Gas Corporation authorized an increase in the amount of its capital stock and the issuance of $4,000,000 of bonds and $1,000,000 of notes (R. 204, 208, 211-217).

On April 7, 1930, an agreement was entered into between Kingston Corporation and Duquesne Gas Corporation (R. 201-203) by which Kingston Corporation undertook to transfer title to the properties hereinbefore referred to in consideration of Duquesne Gas Corporation agreeing to pay an obligation of Kingston Corporation to the Central Hanover Bank & Trust Company in the sum of $3,015,000, and to deliver to Kingston Corporation 535,000 shares of its no par common capital stock, as well as bonds of the par value of $1,300,000. This proposal was accepted by Duquesne Gas Corporation and was carried out.

About the same time, Furlaud & Company, Inc. proposed to Duquesne Gas Corporation to purchase from it the remainder of the bonds of the par value of $2,700,000 and all of its notes for the sum of 90 per cent. of the face value of the bonds and 88 per cent. of the face value of the notes (R. 217-218). Furlaud & Company, Inc. had also subscribed for 139,000 shares of Duquesne Gas Corporation's stock and agreed to pay therefor the sum of 50 cents a share (R. 211).

Mr. Thomas W. Duke, who on behalf of Chapman & Cutler of Chicago and Chapman, Snider, Duke & Radebaugh of New York, acted as counsel for Furlaud & Company and who took charge of the organization of the Duquesne Gas Corporation and the issuing of its securities, was called as a witness on behalf of the plaintiff. He testified that all of the securities of Duquesne Gas Corporation, the bonds, the notes and the stock were issued to Furlaud & Company or to Kingston Corporation, and that

none of these securities was released to Furlaud & Company or to Kingston Corporation until he was certain that every property that was contracted for had been conveyed to Duquesne Gas Corporation and that the said corporation had $365,000 in its treasury as working capital (R. 84, 86, 88).

All of the testimony upon this subject was introduced by the complainant and is uncontradicted.

Let us now see what were the findings of the Trial Court upon this subject.

Judge Knox, referring to the agreement between the Kingston Corporation and Duquesne Gas Corporation says:

> "This instrument provided that Kingston Corporation would acquire the optioned gas properties then in escrow, and turn them over to Duquesne Gas Corporation. The latter, on its part, agreed to pay $3,015,000 to Central Hanover Bank & Trust Company, the amount which Kingston Corporation would be under obligation to pay to the Trust Company. The Duquesne Company further agreed to issue 535,000 shares of its stock and $1,300,000 face value of its first mortgage six per cent. gold bonds to Kingston Corporation, the bonds to be secured by an indenture, dated March 15, 1930, in which the Trust Company was named as Trustee. On April 9, 1930, the following transactions were had at the offices of Central Hanover Bank & Trust Company:
>
> "Maxime H. Furlaud arranged with the bank that for a period of one day the Kingston Corporation should have a credit of $3,015,000, and that Furlaud & Company, Inc. for a like period of time, should be entitled to a credit of $3,379,500.
>
> "When these credits, which were both closely controlled by the Trust Company, had been set up,

Kingston Corporation delivered its certified checks, in the aggregate amount of $2,449,900 to the Equitable Trust Company, Guaranty Trust Company of New York and Central Hanover Bank and Trust Company, respectively. These checks were intended to put the drawees in funds with which to meet drafts which had been drawn against them by the banks in Western Pennsylvania, which held in escrow the several instruments of conveyance by which the gas properties were to be transferred to Duquesne Corporation * * *. (R. 222).

"The banking institutions which received the checks of Kingston Corporation having made telephonic and telegraphic reports of the payments of the purchase money drafts to the banks holding the escrowed conveyances, the latter were straightway delivered and recorded. *This information, being received, Duquesne Gas Corporation proceeded to issue to Kingston Corporation the 535,000 shares of stock and $1,300,000 face value of bonds which were called for by the agreement of April 7, 1930.* Thereupon, Furlaud & Company, Inc. delivered its check to Duquesne Gas Corporation in the sum of $3,379,500. This was supposed to represent the proceeds which the gas corporation was to receive for $2,700,000 par value of its six per cent bonds, its million dollar issue of gold notes, and 139,000 shares of its capital stock. *All of these securities were contemporaneously delivered to Furlaud & Company, Inc.* * * *" (Italics ours.) (R. 222-223.)

There can be no question but that these securities together with the 1,000 shares of stock originally issued to Furlaud & Company, Inc. were all of the securities ever issued by the Duquesne Gas Corporation. The stock and bonds issued to Kingston Corporation were issued and delivered simultaneously and as part of the same transaction.

Let us now see what was the statement of facts of the Court of Appeals upon these transactions.

The Court of Appeals recited the facts of the transaction between Duquesne Gas Corporation in almost the identical language employed by the lower Court (R. 263-267). It then quoted the following from the opinion of the Trial Court: (R. 388-389)

> "At the time that the transaction through which Duquesne Gas Corporation acquired the various gas properties were consummated, and for some time thereafter, Furlaud & Company, Inc. owned every share of its capital stock, and ratified and approved of the whole transaction."

Then follows the language complained of by the petitioner:

> "At the end of these transactions, the two corporations, Furlaud & Company, Inc. and its subsidiary, Kingston Corporation, owned all of the issued common capital stock of the Duquesne Gas Corporation, and all of its bonds and notes. No other person purchased from Duquesne Gas Corporation a share of stock, a bond or a note" (R. 268).

There is no question about the actual facts in this case. They are correctly stated by the Trial Court and by the Court of Appeals.

Petitioner, however, throughout his brief, contends that the properties acquired by Duquesne Gas Corporation were actually paid for out of the money received from the sale by Furlaud & Company, Inc. of Duquesne Gas Corporation securities. In this he differs from the findings of both Courts and from the testimony of Thomas W. Duke, peti-

tioner's own witness upon this subject (R. 84-88). The properties were paid for out of monies furnished by Furlaud & Company, Inc. to its wholly owned subsidiary, Kingston Corporation (R. 81).

Moreover it seems to us to be too clear to justify extended argument that the petitioner's version of the facts could not possibly be true. What Furlaud & Company, Inc. agreed to sell and did sell to the distributing group were issued bonds (R. 178). These bonds could not possibly have been issued and validated until the properties acquired by Duquesne Gas Corporation had been paid for, and the deeds delivered to Duquesne Gas Corporation, and until such deeds and the mortgages securing the bonds and notes (which had been executed in advance) had been recorded; and, even then, not until after Furlaud & Company, Inc. had paid, for the remaining bonds, notes and stock, an amount sufficient to pay the obligation of Kingston Corporation to the Central Hanover Bank & Trust Company and leave in the treasury of Duquesne Gas Corporation the sum of $365,000 as working capital (R. 88).

Until all of these things had been completed, no bonds could have been validated by the trust company and legally released either to Kingston Corporation or Furlaud & Company, Inc. or to any one else. Thomas W. Duke testified that not until all these things had been done were any securities released (R. 88) and so both Courts found (R. 223, 265-266).

It is true that after these bonds had been issued some of them were sold by Furlaud & Company, Inc. to people who had previously agreed to purchase them from it when, as and if issued, and that the proceeds of such sales were used by Furlaud & Company, Inc. to pay off part of the loan due by it to the Central Hanover Bank & Trust Company.

There is in the record only one fact concerning which the findings of the Trial Court and that of the Court of Appeals do not agree, namely, the amount received by Furlaud & Company, Inc. from the sale of the bonds on April 9th, 1930. This amount was fixed by the Trial Court at $3,000,000 (R. 223) and by the Court of Appeals at $1,886,330 (R. 266). The amounts credited to Furlaud & Company's bank account from the sale of bonds were, at the request of the Trial Court, reported to the Court by the witness Halporn who testified from the books of Furlaud & Company, Inc. (R. 128-129), which were in Court and which were offered in evidence (Plaintiff's Exhibits 29 and 30, R. 94, 200). There was at that time present in court Mr. Roger A. McShea, Jr., an accountant employed by the Pennsylvania Public Service Commission, who had made an extensive survey of Furlaud & Company's books (R. 92-93). There was also present an Assistant Vice-President of the Central Hanover Bank & Trust Company who could, at a moment's notice, have verified or disputed the correctness of these figures by merely securing from the bank a statement of the amounts deposited (R. 90-91).

How then did the error of the learned Trial Court occur? The only other testimony upon this subject was that of Eugene P. Brady, a former salesman for Furlaud & Company, Inc., who testified that he was employed to secure commitments for the sale of the bonds of the Duquesne Gas Corporation (R. 73) and that the bond issue was not fully subscribed for (R. 76). When asked to what extent it was subscribed for, he said: "That I would not know, but I should say somewhere in the neighborhood of 75 to 80%" (R. 76). He nowhere testified as to what subscriptions were obtained before nor what amounts were taken up on

April 9, 1930. However, he makes it very clear that not more than eighty per cent. of the bonds were ever subscribed for by the primary group. A secondary group was organized about August 14, 1930 (R. 198-199) and that at that time "I guess there were some $800,000 in bonds left" (R. 103); so that at most the testimony of this witness was to the effect that, between the day of the original offering and approximately August 14, 1930, about eighty per cent. of the bonds had been subscribed for and that the remaining $800,000 were handled through a secondary distributing group and his testimony makes it very clear that he had no real knowledge of the facts.

SUMMARY OF POINTS AND ARGUMENT

1. The facts alleged in the complaint do not show that Duquesne Gas Corporation had a cause of action against any of these defendants.

2. The Trial Court erred in permitting the complainant to introduce testimony tending to show alleged misrepresentations made by Fur[illegible]aud & Company, Inc. to purchasers of securities from it.

3. Notwithstanding the fact that purchasers of securities to whom material misrepresentations might have been made by their vendors and who might have relied thereon to their harm would indubitably have a cause of action against the vendors of such securities, respondent contends that under the facts disclosed in this case neither the Duquesne Gas Corporation nor its receiver could have been injured or could have acquired a cause of action as a result thereof.

4. Under the facts of this case the plaintiff in his capacity of receiver has no greater rights or powers than the corporation itself would have.

5. The contention of the petitioner that the corporation was powerless to render itself insolvent by surrender to the defendants of its right to hold them accountable to it for the proceeds which came into the hands of defendants from the sale of the securities of the corporation, is not only not within the issues presented by the complaint, but under the facts of this case is unsound.

6. The question presented by petitioner under Point VI of his brief, having been raised for the first time upon the second argument of the appeal of this case, could not in any event be considered because

(1) There is no allegation in the complaint under which this issue, if sound, could have been raised;

(2) It is in direct conflict with the theory upon which the case was tried in the lower court.

7. The Trial Court properly dismissed the complaint as to the defendants Byron Corporation and Chaucer Corporation.

8. The defendant Furlaud is not personally liable in this case in any event.

9. The complaint affirmatively shows that complainant had no title to any cause of action that could have been asserted by Duquesne Gas Corporation.

POINT I

THE FACTS ALLEGED IN THE COMPLAINT DO NOT SHOW THAT DUQUESNE GAS CORPORATION HAD A CAUSE OF ACTION AGAINST ANY OF THESE DEFENDANTS.

We shall paraphrase the allegations contained in the complaint.

The first seven paragraphs (R. 4-6) are devoted to allegations showing the jurisdiction of the Court in relation to the parties, that Carlos Reuter and Maxime H. Furlaud owned all of the stock of Furlaud & Company, Inc., that Furlaud & Company, Inc. was an investment banking house which in turn owned all of the stock of Kingston Corporation and through Kingston Corporation acquired options on certain properties in Pennsylvania, that after the options had been acquired Furlaud & Company, Inc. caused another corporation, Duquesne Gas Corporation, to be organized and that then Furlaud & Company, Inc. owned all of the stock issued by that corporation, that Duquesne Gas Corporation authorized the issuance of secured bonds in the face amount of $4,000,000 and secured notes in the face amount of $1,000,000, and 675,000 shares of no par value stock.

The "Eighth" paragraph (R. 6-7) alleges that Furlaud & Company, Inc., as a banking house of issue, made a public offering of the bonds and notes and stated in the bond and note circulars that the securities were (or are) issued by the corporation in connection with the acquisition of properties and to provide cash for development, extensions and other corporate purposes. THERE IS NO ALLEGATION ANYWHERE IN THE COMPLAINT THAT THESE REPRESENTA-

TIONS OR, IN FACT, ANY REPRESENTATIONS THAT WERE MADE, WERE NOT IN ALL RESPECTS TRUE.

The "Ninth" paragraph (R. 7) alleges that Furlaud & Company, Inc. had arranged for the acquisition by Duquesne Gas Corporation of various properties, the aggregate price being $2,572,989, that the properties were to be conveyed to Duquesne Gas Corporation in consideration of the payment by Duquesne Gas Corporation of said sum and that such sum was paid out of the proceeds of the sale of the bonds and securities.

The "Tenth", "Eleventh", "Twelfth" and "Thirteenth" paragraphs (R. 7-9) are devoted to showing the amount for which the securities were sold and that the difference between that amount, and the cost of the property and $365,000, was retained by Furlaud & Company, Inc. and/or some of the defendants.

The "Fourteenth" (R. 9) merely alleges that these defendants or some of them stood in a fiduciary relationship to Duquesne Gas Corporation.

The "Fifteenth" (R. 9) summarizes the mathematics of all of the transactions referred to.

Unless, therefore, the "Eighth" paragraph of this complaint can be so construed as to allege that Furlaud & Company, Inc. were disposing of the securities as agents of Duquesne Gas Corporation, there is nothing in this complaint that could be construed as alleging a cause of action against any one. Attention is called to the fact not only that no such allegation is made in these paragraphs of the complaint but that on the contrary in this paragraph Furlaud & Company, Inc. is described as a house of issue.

A house of issue is, of course, a house which having purchased or underwritten a security first offers it for sale to the public. Sometimes corporations offer their own securities directly to the public and employ banking houses

to make the offering for them, but in such cases the banking house is not acting as a house of issue but as an agent or broker.

However, complainant was not content to stand on the first fifteen paragraphs of his complaint, but in the "Sixteenth" paragraph (R. 9-12) he entered into a detailed categorical statement of the steps by which the transaction was carried into effect. This paragraph completely negatives any theory that Furlaud & Company, Inc. was acting as agent for Duquesne Gas Corporation in selling securities or that Duquesne Gas Corporation purchased the properties from any one other than Kingston Corporation.

The "Sixteenth" paragraph shows that Kingston Corporation acquired options for the purchase of various properties, that Furlaud and Reuter caused Duquesne Gas Corporation to enter into a contract with Furlaud & Company, Inc. for the sale by Duquesne Gas Corporation to Furlaud & Company, Inc. of $2,700,000 of its bonds and $1,000,000 of its notes, that an agreement of reorganization between Duquesne Gas Corporation and Kingston Corporation was executed and under said agreement Kingston Corporation agreed to convey said property to Duquesne Gas Corporation and Duquesne Gas Corporation agreed to pay $3,015,000, stated to be the amount which Kingston Corporation would be obligated to pay to Central Hanover Bank & Trust Company, and to issue and deliver to Kingston Corporation 535,000 shares of its common stock and $1,300,000 in principal amount of its 6% Mortgage Convertible Gold Bonds, and that Kingston Corporation declared a dividend in kind to its stockholders (Furlaud & Company, Inc.) of said $1,300,000 in face amount of bonds.

In other words, the plaintiff alleges in effect that Furlaud & Company, Inc. purchased the $1,000,000 in notes,

$2,700,000 in bonds, and 140,000 shares of stock at a price that is nowhere challenged by the petitioner, and that Kingston Corporation transferred to Duquesne Gas Corporation property which cost it $2,572,989, in consideration of the assumption by Duquesne Gas Corporation of a debt of Kingston Corporation amounting to $3,015,000 and the issuance to Kingston Corporation of bonds of the face value of $1,300,000 and 535,000 shares of common stock of no par value.

There is even no allegation in the complaint that the property conveyed by Kingston Corporation to Duquesne Corporation was not fairly worth the amount paid for it by Duquesne Gas Corporation.

Obviously this complaint affirmatively shows that Furlaud & Company, Inc. and its wholly owned subsidiary, Kingston Corporation, on the one hand, entered into an agreement with Duquesne Gas Corporation, which, at the time of the agreement, was a wholly owned subsidiary of Furlaud & Company, Inc., by the terms of which Duquesne Gas Corporation acquired certain property and certain monies and in exchange therefor agreed to, and did deliver to Furlaud & Company and Kingston Corporation all of its stock that was ever issued and all of its securities that were ever issued. The complainant alleges that Furlaud & Company, Inc., sold these securities, but there is no allegation in the complaint that in making these sales they made any misrepresentation of any kind to the purchasers of the securities.

We respectfully insist that the facts alleged in this complaint do not constitute a cause of action of any kind.

As we discuss the questions of law involved under Point III of this brief, we refer to our argument there in support of our contention here.

POINT II

THE TRIAL COURT ERRED IN PERMITTING THE COMPLAINANT TO INTRODUCE TESTIMONY TENDING TO SHOW ALLEGED MISREPRESENTATIONS MADE BY FURLAUD & COMPANY, INC. TO PURCHASERS OF SECURITIES FROM IT.

Attention of this Court is called to the following facts:

1. After the amended complaint was served in this case the defendants, Maxime H. Furlaud and Kingston Corporation, made an application under Equity Rule 20 to require the complainant to make a further and better statement of the nature of his claim by setting forth definitely and specifically the ultimate facts upon which it was claimed (1) that the defendants Furlaud and Reuter caused the proceeds of the sale of the bonds and notes to be diverted from the Duquesne Gas Corporation and (2) that the defendants fraudulently misappropriated funds and diverted monies from the proper uses of the Duquesne Gas Corporation (R. 13-15).

This motion was opposed by the solicitors for the complainant. In the affidavit submitted by Mr. Ralph Royall, the deponent states: "It is submitted that a reading of the amended bill of complaint will show that, although the proceedings taken by these defendants in diverting and misappropriating the assets of Duquesne Gas Corporation were involved and elaborate, they are clearly set forth in chronological order.. It is also submitted that such facts so alleged can bear only the ultimate inference that the defendants stood and stand in a fiduciary relationship to the defendant Duquesne Gas Corporation and that in such relationship

they are accountable to the corporation and to its Receiver for all the monies coming into their hands or the hands of any of them from the sale of the securities of Duquesne Gas Corporation, and the bill alleges such fiduciary relationship" (R. 26).

So it appears that complainant, after having been given this opportunity to again amend his complaint, elected to stand on his complaint as filed.

Attention is further called to the fact that the amended bill of complaint does not contain a single allegation to the effect that there was any overvaluation of the properties acquired by Duquesne Gas Corporation or that any misrepresentations of value or of anything else were made to anyone.

2. The opinion of the Trial Court is based upon his findings that the circulars and the advertisements appearing in the New York Times relating to the bonds and the notes of the Duquesne Gas Corporation stated that the property of the Corporation had an aggregate appraised value (including working capital of $365,000) amounting to $7,038,000 (R. 224) although certain of the properties which were appraised by the firm of Mattison, Davey & Winters at $4,929,787 cost only $1,200,000 and were greatly overvalued (R. 220); and, finally, that the value of the properties were grossly and fraudulently misrepresented to the public (R. 224).

The entire decision of the Trial Court is based on the theory that the purchasers of the bonds and notes of the Duquesne Gas Corporation must have been misled by the so-called misrepresentations of the value of the properties of the Duquesne Gas Corporation. One would conclude from the opinion that the gravamen of the complaint was

the misrepresentations set forth above and that allegations with respect thereto were set out in the bill of complaint.

The only reference in the complaint to any statement in the circulars issued in connection with the distribution of the bonds and notes appears in paragraph "Eighth" and it is merely alleged that it was stated in said circulars that the bonds and notes were (are) issued by the corporation in connection with the acquisition of properties and to provide cash for development, extensions and other corporate purposes (R. 7).

There is no allegation that these statements were false or that they were material or that they misled any one.

Nowhere in the amended complaint is there a single allegation which has been held to be an essential part of actionable fraud.

It is evident that the theory of the complainant's case, as set forth in the amended complaint, is not based on any claimed misrepresentations of facts or overvaluation of properties. Any such theory was a pure afterthought of the pleader. The complainant's solicitors repeatedly insisted and the Court found that the gravamen of their suit was that the securities of Duquesne Gas Corporation came into their hands in a fiduciary capacity and that a large portion of the funds received by the defendants from the sale of such securities was diverted and misappropriated from the treasury of the Duquesne Gas Corporation (R. 219).

Not a suggestion was ever made, until after the trial was in progress, that any claimed misrepresentation furnished the gravamen of the cause. No such interpretation can be spelt out of the amended complaint.

At the trial, however, the complainant produced Charles C. Nuss, Walter C. Krog, Lyon F. Terry and Cyrus C. Robbins and through them introduced evidence tending to prove that the appraisal contained in the circulars and the advertisements appearing in the New York "Times" relating to the bonds and notes of Duquesne Gas Corporation had been fraudulently made and grossly overvalued the properties. This testimony tended to show that the fair market value of the property was much less than that set out in the appraisal and that the property cost even less than that. All of this testimony was strenuously objected to by the defendants (R. 57-60, 61, 62, 63, 109, 113).

The objections and exceptions were so numerous that counsel for complainant three times stated that defendant would be considered as having a general objection to all testimony of this general character (R. 53, 54, 69) and the Court stated (R. 113):

> "Yes, you may have an exception to this line of testimony".

The defendants pled surprise and stated to the Court that they were not prepared to meet the testimony upon this issue (R. 60) and generally did everything they could do to protect themselves against the introduction of the testimony.

If the complaint in this case states a cause of action at all, which we greatly doubt, it is a cause of action based either upon the contention that Furlaud & Company, Inc. and Kingston Corporation were acting as trustees or agents for Duquesne Gas Corporation in acquiring the properties transferred to it, and as such agents or trustees were under the obligation to turn the properties over to the corporation at cost, or that the bonds and notes issued by the corpora-

tion were entrusted to them as agents for sale and that they had failed to account.

Under neither of these theories was any such testimony relevant, material, or competent. If the defendants, or any of them, were acting as agents for Duquesne Gas Corporation in disposing of these securities, they were, of course, obliged to account for the proceeds of the sale of such securities.

If the defendants, or any of them, were merely acting as agents for Duquesne Gas Corporation in purchasing the properties for it, they were, of course, under obligation to turn the properties over to Duquesne Gas Corporation without making any secret profits upon the transaction. That they could have made no secret profits indubitably appears from the fact that Furlaud & Company, Inc. owned Duquesne Gas Corporation. It, Duquesne Gas Corporation, was not organized until *after* these options had been acquired and, when organized, was completely owned by Furlaud & Company, Inc. There could, of course, have been no secret profits as any transaction between Furlaud & Company, Inc. and Duquesne Gas Corporation, which was a mere instrumentality of Furlaud & Company, Inc.

The learned Trial Court did not in express terms overrule the decision of this Court in *Old Dominion Copper Co. v. Lewisohn*, 210 U. S. 206. In fact, in part he recognized its binding force (R. 232).

He did, however, base his opinion upon the theory that misrepresentations made to the purchasers of securities by the promoters of a corporation who had acquired them from the corporation in the manner that these were acquired created an obligation which, even if the corporation itself could not enforce, its Receiver in his representative capacity could. As we discuss this question of law elsewhere,

we shall make no comment upon it here further than to say that it demonstrates the proposition that, since this testimony was not admissible, it was extremely prejudicial. We are forced to ask where in the Complaint is there any allegation under which this testimony could be admitted. If this testimony were eliminated from this record, is it not obvious that no one would have had the slightest cause for complaint?

No principal of equity jurisprudence is more firmly fixed than that, as in law, so in equity, the *allegata* and *probata* must correspond and that the plaintiff, in equity, cannot recover if his proof does not harmonize with the allegations in his bill. In equity proceedings a party is not allowed to state one case in his pleadings and make out a different one in his proof. Averments without proofs and proofs without averments are alike unavailing. Any other rule would do away with the necessity for pleadings, and lead to surprise and unfairness on the trial.

In the case of *Foster* v. *Goddard,* 1 Black 506, the Supreme Court of the United States, per Mr. Justice Swayne, said (p. 518):

> "In equity proceedings the proofs and allegations must agree. A party can no more succeed upon a case proved, but not alleged, than upon a case alleged, but not proved. *Simms* v. *Guthrie,* 9 Cranch 19; *Harrison* v. *Nixon,* 9 Pet. 483; *Boone* v. *Chiles,* 10 Pet. 178; *Trip* v. *Vincent,* 3 Barb. C. H. 613; *Bank of U. S.* v. *Shultz,* 3 Ohio R. 61; *Sadler* v. *Glover,* 5 Dana 552; *Breckenridge* v. *Ormsby,* 1 J. J. Marsh 236."

In *Harrison* v. *Nixon,* 9 Pet. 483, Mr. Justice Story stated (p. 503):

"Every bill must contain in itself sufficient matters of fact, *per se,* to maintain the case of the plaintiff; so that the same may be put in issue by the answer, and established by the proofs. The proofs must be according to the allegations of the parties; and if the proofs go to matters not within the allegations, the court cannot judicially act upon them as a ground for its decision; for the pleadings do not put them in contestation. The *allegata* and the *probata* must reciprocally meet and conform to each other."

In the case of *Crocket* v. *Lee,* 7 Wheat. 522, Mr. Chief Justice Marshall, in discussing a similar situation, said (p. 526):

"The counsel for the appellant says it would be monstrous, if, after the parties have gone to trial on the validity of the entry, and have directed all their testimony in the Circuit Court to that point, their rights should be made to depend in the appellate court on a mere defect in the pleadings, which had entirely escaped their observation in the Court where it might have been amended, and the non-existence of which would not have varied the case.

"The hardships of a particular case would not justify this tribunal in prostrating the fundamental rules of a court of Chancery—rules which have been established for ages, on the soundest and clearest principles of general utility. If the pleadings in the cause were to give no notice to the parties or to the Court of the material facts on which the right asserted was to depend, no notice of the points to which the testimony was to be directed, and to which it was to be limited; if a new case might be made out in proof, different from that stated in the pleadings, all will perceive the confusion and uncertainty which would attend legal proceedings, and the injustice

which must frequently take place. The rule that the decree must conform to the allegations, as well as to the proofs of the parties, is not only one which justice requires, but one which necessity imposes on Courts."

In *Garrett* v. *Louisville & N. R. Co.*, 235 U. S. 308, at page 312, this Court says:

"Where any fact is necessary to be proved in order to sustain the plaintiff's right of recovery, the declaration must contain an averment substantially of such fact in order to let in the proof. Every issue must be founded upon some certain point, so that the parties may come prepared with their evidence, and not be taken by surprise, and the jury may not be misled by the introduction of various matters. *Bank of United States* v. *Smith*, 11 Wheat. 171, 174 6 L. Ed. 443, 444; *Minor* v. *Mechanics' Bank*, 1 Pet. 46, 67, 7 L. Ed. 47, 56; *De Luca* v. *Hughes*, 96 Fed. 923, 925; *Rose* v. *Perry*, 8 Yerg. 156; *Citizens' Street R. Co.* v. *Burke*, 98 Tenn. 650, 40 S. W. 1085, 2 Am. Neg. Rep. 459; 1 Chitty, P. 270. Although the same precision of statement is not required as in pleadings at law, nevertheless it is held to be absolutely necessary that in bills of equity such a convenient degree of certainty should be adopted as may serve to give the defendant full information of the case which he is called upon to answer. Every bill must contain in itself sufficient matters of fact, *per se*, to maintain the plaintiff's case; and if the proofs go to matters not set up therein the court cannot judicially act upon them as a ground for decision, for the pleadings do not put them in contestation. *Harrison* v. *Nixon*, 9 Pet. 483, 503, 9 L. Ed. 201, 208; Dan. Ch. P. & Pr. 368."

"The plaintiff's declaration contains no positive averment of pecuniary loss to the parents for whose

benefit the suit was instituted. Nor does it set out facts or circumstances adequate to apprise the defendant with reasonable particularity that such loss in fact was suffered."

See also:

Henry v. *Suttle,* 42 Fed. 91;
Dashiell v. *Grosvenor,* 66 Fed. 334;
Finefrock v. *Kenova Mine Car Co.,* 22 Fed. (2d) 627, at page 634;
Babbitt v. *Dotten,* 14 Fed. 19.

We respectfully submit that the Trial Court committed reversible error in receiving and considering this testimony.

POINT III

NOTWITHSTANDING THE FACT THAT PURCHASERS OF SECURITIES TO WHOM MATERIAL MISREPRESENTATIONS MIGHT HAVE BEEN MADE BY THEIR VENDORS AND WHO MIGHT HAVE RELIED THEREON TO THEIR HARM WOULD INDUBITABLY HAVE A CAUSE OF ACTION AGAINST THE VENDORS OF SUCH SECURITIES, RESPONDENT CONTENDS THAT UNDER THE FACTS DISCLOSED IN THIS CASE NEITHER THE DUQUESNE GAS CORPORATION NOR ITS RECEIVER COULD HAVE BEEN INJURED OR COULD HAVE ACQUIRED A CAUSE OF ACTION AS A RESULT THEREOF.

Statement of Facts

No controversy exists as to the actual facts involved. They are uncontradicted in the evidence. They are recited

in the findings of the Trial Court and in those of the Court of Appeals.

They are substantially as follows:

Furlaud & Company, Inc. was engaged in the business of buying and selling corporate securities (R. 219).

Kingston Corporation was a wholly owned subsidiary of Furlaud & Company, Inc. (R. 113). In the Fall of 1929 and early in 1930, Kingston Corporation acquired options upon nine gas properties located in Western Pennsylvania and elsewhere. The agreed purchase price of these properties amounted to $2,572,989 (R. 51-52, 59).

Subsequently and on February 21st, 1930, Duquesne Gas Corporation was organized by Furlaud & Company, Inc. with an original authorized capital of 1,000 shares of no par value (R. 22). This stock was subscribed for and acquired by Furlaud & Company, Inc. for the sum of $500 in cash.

Thereafter, on or about March 5th, 1930 Duquesne Gas Corporation "the entire capital stock of which was held by Furlaud & Company, Inc. or its nominees, authorized issue of four million dollars of six per cent. gold bonds, and the one million dollars of 6½ per cent. notes, to be secured respectively by first and second mortgages upon its properties. The company's authorized capital was also increased from 1,000 to 675,000 shares, without par value" (Judge Knox's opinion, R. 221).

> "On April 7, 1930, Duquesne Gas Corporation and Kingston Corporation entered into what was termed an 'Agreement of Reorganization.' This instrument provided that Kingston Corporation would acquire the optioned gas properties then in escrow, and turn them over to Duquesne Gas Corporation.

The latter, on its part, agreed to pay $3,015,000 to Central Hanover Bank & Trust Company, the amount which Kingston Corporation would be under obligation to pay to the Trust Company. The Duquesne Company further agreed to issue 535,000 shares of its stock and $1,300,000 face value of its first mortgage six per cent. gold bonds to Kingston Corporation, the bonds to be secured by an indenture, dated March 15, 1930, in which the Trust Company was named as Trustee. *On April 9, 1930, the following transactions were had at the offices of Central Hanover Bank & Trust Company:*

Maxime H. Furlaud arranged with the bank that for a period of one day the Kingston Corporation should have a credit of $3,015,000, and that Furlaud & Company, Inc. for a like period of time, should be entitled to a credit of $3,379,500.

"When these credits, which were both closely controlled by the Trust Company, had been set up, Kingston Corporation delivered its certified checks, in the aggregate amount of $2,449,900 to the Equitable Trust Company, Guaranty Trust Company of New York and Central Hanover Bank and Trust Company, respectively. These checks were intended to put the drawees in funds with which to meet drafts which had been drawn against them by the banks in Western Pennsylvania, which held in escrow the several instruments of conveyance by which the gas properties were to be transferred to Duquesne Gas Corporation * * *" (italics ours) (Judge Knox's opinion, R. 222).

"The banking institutions which received the checks of Kingston Corporation having made telephonic and telegraphic reports of the payments of the purchase money drafts to the banks holding the escrowed conveyances, the latter were straightway delivered and recorded. This information, being re-

*ceived, Duquesne Gas Corporation proceeded to issue to Kingston Corporation the 535,000 shares of stock and $1,300,000 face value of bonds which were called for by the agreement of April 7, 1930. * * *"* (Judge Knox's Opinion, R. 222-223) (Italics ours).

In order to provide the funds required for the closing and marketing operations, Furlaud & Company, Inc. borrowed on three time loans the aggregate additional amount of $1,500,000, to wit, $700,000 from the Chatham & Phoenix National Bank & Trust Company, $500,000 from the Pacific Trust Company and $300,000 from the Hibernia Trust Company. Some of these sums so borrowed were immediately credited to Furlaud & Company's account at the Central Hanover Bank & Trust Company (R. 114).

As a result of these transactions, Kingston Corporation transferred substantially all of its properties to Duquesne Gas Corporation, receiving in exchange therefor 535,000 shares of the common capital stock of Duquesne Gas Corporation, first mortgage bonds of Duquesne Gas Corporation of the face value of $1,300,000 and Duquesne Gas Corporation assumed Kingston Corporation's obligation to the Central Hanover Bank & Trust Company in the sum of $3,015.000.

Concurrently, Furlaud & Company, Inc. purchased from Duquesne Gas Corporation the remaining $2,700,000 bonds at $90, the $1,000,000 notes at $88 and 139,000 shares of common stock at 50 cents per share, paying therefor the sum of $3;379,500 (R. 85, 217-218).

Out of this sum, Duquesne Gas Corporation paid the sum of $3,015,000 to the Central Hanover Bank & Trust Company representing the amount of Kingston Corporation's obligation to that bank which Duquesne Gas Corpo-

ration had assumed (R. 78, 82, 355, 356). The balance remained in the treasury of the Duquesne Gas Corporation (R. 78, 88).

As a result of these transactions, Furlaud & Company, Inc. and its subsidiary acquired every share of the common capital stock of Duquesne Gas Corporation, issued and outstanding, and every bond and note of that corporation, and the corporation did not owe to any other person any obligation of any kind. (R. 226).

No other person purchased from Duquesne Gas Corporation a single share of stock or a bond or a note.

In this transaction no fraud of any kind could have been perpetrated on Duquesne Gas Corporation because, as stated by the Trial Court:

> "At the time that the transactions through which Duquesne Gas Corporation acquired the various gas properties were consummated, and for some time thereafter, Furlaud & Company, Inc., owned every share of its capital stock, and ratified and approved of the whole transaction" (Judge Knox's Opinion, R. 231-232).

Were it not for the decision of the Trial Court, it would hardly seem necessary to cite authorities to establish the proposition that where the owners of property create a corporation, transfer their property to it, and receive in exchange all of the stock of that corporation and all of the bonds and notes ever issued by it, and, at the time of the transfer, no other person was interested in the corporation either as stockholder or creditor, no injury could result to any one whatsoever.

Under such circumstances, the corporation entered into the transaction with full knowledge of all facts. The ven-

dors and the vendee of the property so conveyed were one and the same, both in equity and in fact.

It seems abundantly clear that this Court in the case of *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206, the Circuit Court of Appeals for the Second Circuit in the case of *Ball* v. *Breed*, 294 Fed. 227 (certiorari denied, 264 U. S. 584), and the Court of Appeals of the State of New York in the case of *Blum* v. *Whitney*, 185 N. Y. 232, have held and it is now the well established rule of law that neither a corporation nor its receiver has any cause of action against the organizers of such corporation for the recovery of profits made by such organizers either in the sale of properties to it or growing out of the sale of the securities of that corporation where the organizers, at the time of the transaction between them and the corporation, were the owners of all of the authorized and outstanding stock of said corporation.

It indubitably follows, therefore, that Duquesne Gas Corporation acquired no cause of action against any of these defendants on account of transactions which resulted in its organization and the original issue of its stock and securities.

If, therefore, this receiver had any cause of action against any of these defendants it must have resulted from some transaction other than those between the corporation and its organizers.

However, petitioner contends:

That before actually concluding the said transactions with Duquesne Gas Corporation, Furlaud & Company, Inc. organized a syndicate of which it became manager and from which it secured commitments to purchase certain portions of the bonds of Duquesne Gas Corporation, if, when and as issued (R. 73-74, 119-122, 178-180).

That this syndicate in turn organized a distributing group and issued circulars advertising these bonds which stated:

That they were secured by a mortgage covering properties which, including working capital of $365,000, had been appraised at an aggregate value of $7,038,000 (R. 224), and

That the appraisal made by Mattison, Davey & Winters was not a sound one and did not reflect the true value of the property and that, as a result of these additional facts, a cause of action did accrue to the corporation or to its Receiver.

We think we have shown in Point II of this brief that the admission of the testimony upon this subject was erroneous. The Trial Court, however, not only makes this testimony the basis of his opinion and decision but makes the following comment:

> "Defendants, it may be remarked, offered no evidence to rebut the conclusion that is compelled by Plaintiff's proof" (R. 224).

We feel constrained at this point to say that this case was actually on trial before defendants had any notice that the Petitioner intended to assert that any misrepresentations had been made to the purchasers of securities.

It would at that time have been impossible to have properly prepared to rebut the testimony offered without adjourning the trial.

The party who had made the appraisal were largely engaged in the southern and mid-continent oil fields (R. 71). In order to properly prepare for the trial of this issue, it would have been necessary for counsel to present their testimony and that of other engineers upon the question of the

value of these properties. It would also have been necessary to have prepared testimony, which counsel is advised could have been secured, to show the interest of the adverse witnesses and engineers in making it appear that the properties had as little value as possible. It would have been necessary to make a breakdown and analysis of the report of the certified public accountants to show the profits earned by these properties in 1929 and 1930 and to have presented a detailed record of the effect, not only upon Duquesne Gas Corporation but upon its customers who purchased large quantities of natural gas, of the depression in their business which was already apparent by the end of 1930.

Moreover, defendants were not only confident that all of the testimony offered upon the subject of overvaluation and misrepresentation was incompetent and irrelevant and immaterial but also, because of the fact that the Trial Court admitted practically everything that was offered, defendants were confident that in considering the testimony presented the learned Trial Court would exclude from his mind all such incompetent testimony. For these reasons and because they had no witnesses available with which to effectively meet this issue at that time, they elected to ignore this testimony.

Argument

If, for the purpose of this argument, we assume that the representations contained in these circulars were not in fact true and even that they were relied upon by the purchasers of the bonds and notes who acted upon such representations to their harm (although as we have shown there is no testimony to that effect in the record), we must then inquire what actionable injury resulted therefrom to the

corporation upon which this receiver could rely as a basis for a recovery against these defendants.

At the time of the sale of these properties by Kingston Corporation to Duquesne Gas Corporation, Furlaud & Company, Inc. owned all of the stock of Duquesne Gas Corporation. As the result of the sale of this property by Kingston Corporation, and the payment by Furlaud & Company, Inc. of a sum of money, Furlaud & Company, Inc. and its wholly owned subsidiary, Kingston Corporation, acquired every share of stock, every note and every bond ever issued by Duquesne Gas Corporation.

Mr. Justice Holmes in the case of *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206, at page 212, says:

> "At the time of the sale to the plaintiff, then, there was no wrong done to anyone. Bigelow, Lewisohn, and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in exchange for their conveyance of their land. * * * *If there was a wrong, it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation nunc pro tunc, but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. For it is only by virtue of the innocent subscribers' position and the promoter's invitation that the corporation has any pretense for a standing in court. If the promoters, after starting their scheme, had sold their stock before any subscriptions were taken, and then the purchasers of their stock, without notice, had invited the public to come in, and it did, we do not see how the company*

> *could maintain this suit. If it could not then, we do not see how it can now.*" (Italics ours.)

We think this statement of the law alone should have disposed of this case.

The Trial Court obviously confused the situation in this case with such as occurred in the case of *Gates* v. *Megargel,* 266 Fed. 811. The Trial Court in his opinion refers to this case and says:

> "In a sense, the situation is analogous to those in which promoters have been held liable for profits accruing to themselves through the misrepresentation of the true value of property conveyed to a corporation, when reliance upon such misrepresentation has been had by innocent purchasers of the stock of the corporation." (R. 221).

The distinction between the situation that existed in the *Megargel* case and that which exists in this case hardly requires further comment than the mere statement that in the *Megargel* case, suit was brought, not by the corporation or by its receiver, but by members of the syndicate. Obviously, in the cause of action referred to in that case, the syndicate members were the persons aggrieved and were not only the proper persons *but the only persons* who could maintain a cause of action growing out of such facts.

Petitioner, at page 22 of his brief, refers to *Yeiser* v. *United States Board & Paper Co.,* 107 Fed. 340, 344 (C. C. A. 6th 1901), and the case of *New Sombrero Phosphate Co.* v. *Erlanger,* L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rep. 436 (1877), and seems to contend that these cases limit the doctrine of the *Lewisohn* case.

Both of these cases were urged upon the Supreme Court in the *Lewisohn* case, and were disposed of by Mr. Justice Holmes on the ground that in those cases, at the very time that the promoters carried through their transactions, there were in existence innocent non-assenting stockholders to whom no disclosure of the true situation had been made. These cases are proper authorities to support the decision of *Davis* v. *Las Ovas*, 227 U. S. 80 which also involved the presence of innocent nonassenting stockholders at the very time that the transaction between the promoters and the corporation was closed but can have no application to a case in which the corporation had no dealings of any kind with any one other than its organizers.

In the case of *Ball* v. *Breed*, supra, one Tippenauer had by contract acquired options to purchase properties in Haiti. He entered into two contracts with certain bankers who organized a corporation known as the H. A. Company. By one of these contracts he agreed to transfer his options and holdings to the corporation in exchange for 60,000 shares of its common and founders' stock and the sum of $1,600,000—$500,000 in cash and the balance when a fund for that purpose should become available. By the second agreement, it was provided in effect that what Tippenauer was really to receive was $500,000 and 2500 shares of its common and 2500 shares of its founders' stock and that his rights to the remaining $1,100,000 and 55,000 shares of common and founders' stock should be transferred to the bankers, who were undertaking to finance the corporation. These agreements were executed on October 24th, 1916.

Immediately thereafter the bankers organized a syndicate of which the bankers were the syndicate managers

and to which the bankers were to sell if, when and as issued 55,000 shares of preferred stock of the said H. A. Company, 27,500 shares of common stock and 27,500 shares of founders' stock for the total price of $5,225,000.

The bankers thereupon made a call upon the syndicate of 20% and, as syndicate managers, received the sum of $1,050,000.00 in cash. In January, 1917 they organized the H. A. Corporation, in February, 1917, they subscribed for all of the preferred stock in their own name, utilized the amount which they received from the syndicate in providing the corporation with funds to pay Tippenauer his $500,000 and certain other sums which were required to organize the corporation amounting to $54,000 and to retain the amount of working capital that it was agreed the corporation should have. They used the credit of $1,100,000 to release the proportionate amount of preferred stock to which they were entitled under the agreement. By these means the Bankers acquired a sufficient amount of preferred stock, common stock and founders' stock with which to carry out their obligations to the syndicate and leave them a substantial profit.

The H. A. Company subsequently went into the hands of Receivers and the Receivers brought suit alleging that, as a result of these transactions, the Bankers had received a secret profit of $1,100,000 which they did not make known.

The Circuit Court of Appeals for the Second Circuit, says on page 231:

> "In the case at bar, suit is brought by the receiver on the theory that the profit made by the promoters was without knowledge and consent of the corportaion, and that the corporation does not consent, if any existing stockholder is ignorant of

the transaction and of the so-called secret profit. The ultimate fact upon which decision must rest is that the alleged secret profit was a matter of contract between Tippenauer and the bankers, and as these owned all the preferred and all of the common and all of the founders' stock which was either subscribed for or intended to be issued, there were no persons having any rights to receive stock from the corporation. Thus there were no innocent stockholders. In other words, there was no fraud upon the corporation."

Continuing at page 232, the Court very carefully distinguishes cases like *Davis* v. *Las Ovas*, 227 U. S. 80 from cases like this, saying of the *Las Ovas* case:

> "In *Davis* v. *Las Ovas*, 227 U. S. 80, 33 Sup. Ct. 197, 57 L. Ed. 426, the court held that, where the true consideration of a syndicate purchase is concealed, and the property is conveyed at a higher figure in shares of stock to a corporation *whose stock is held partly by members of the syndicate and partly by others*, and the necessary increase of shares to pay for the property goes to some of the syndicate promoters as a secret profit, the corporation may maintain an action to require those obtaining the shares to surrender them for cancellation." (Italics ours.)

Continuing, later on the same page:

> *"In the case at bar, there is no such state of facts. It is nowhere alleged as a fact, nor can it be inferred that there were any innocent stockholders at the time of the transaction complained of. If, then, there was a fraud, it was not against the corporation, and a cause of action, if any, is personal to the purchasers of the stock.* The fraud, if any, is what

has been called a subsidiary fraud not affecting the corporation. Allowing to the complaint the most favorable inference, all that can be said is, as concisely stated by the District Court, that:

> 'These transactions between the defendants and the subscribers to their syndicate had nothing to do with the formation of the corporation, the syndicate subscribers only agreed with the syndicate managers to take what the managers get for them, and they got it through the managers'." (Italics ours.)

Application was made to the Supreme Court of the United States for a writ of certiorari in *Ball* v. *Breed*, 264 U. S. 584. In the application for the writ and in the brief attached thereto the Petitioner urged the very question here presented upon the Supreme Court of the United States. On page IV of the Petition, the Plaintiff stated:

> "The two essential questions, more fully developed later, are: (1) Where a promoter enlists his syndicate subscribers, *puts their cash contribution into the corporation's capital, and thereafter sells property to it at a profit without disclosure of such profit to the corporation or to such subscribers, can he escape liability to account to the corporation for such profit, through the device of postponing the distribution of stock certificates to his subscribers until after the sale?* (2) Where a promoter disregards his established obligation as a fiduciary to disclose his profit to his syndicate subscribers and to his corporation, and even conceals such profit by false entries upon the corporation's books, is he immune from accountability to the corporation through merely having employed the device of inserting in his promotion documents a recital that his acquisition of stock for the syndicate will be by purchase from himself?" (Italics ours.)

On page IX of the Petition, the plaintiff contended:

> "Second, it (the decision of the Circuit Court of Appeals) fails to apply the principle established by this Court: that where the promoter of a corporation, before organizing the corporation, *enlists from various persons funds which are to form the corporation's capital, with which funds the corporation, when organized, buys property,* the promoter owes to such persons and to the corporation the duty to disclose fully the profit which he is making out of such sale of such property to the corporation." (Italics ours.)

The application for the writ was denied by this Court.

The Court of Appeals of the State of New York in the case of *Blum* v. *Whitney,* 185 N. Y. 232, at page 244, quotes from the case of *Tompkins* v. *Sperry, Jones & Co.,* 96 Md. 560, as follows:

> "It is a misuse of terms in the present case to say that Sperry and Jones stood in a fiduciary relation to the company at the time they made the contracts with the brewers, or when they turned property into the company in payment of its stock and bonds. *They at that time held all of its stock and were the sole owners of the company. They were in equity the company itself."* (Italics ours.)

Even in the State of Massachusetts where the rule on this general subject is not in complete harmony with the Federal rule, it is now well settled that a corporation cannot recover profits made by promoters in selling to it their own property, provided such promoters are or become the original subscribers of *all of the shares of capital stock contemplated as a part of the scheme of promotion, as is admittedly true in this case.*

Hays v. *The Georgian,* 280 Mass. 10.

In that case, speaking of the decision of the lower Court, the Supreme Court of Massachusetts says (p. 20):

> "In substance and effect, this is a succinct statement of the principle that, if the promoters and those acting in concert with them, are the *original subscribers to the entire capital stock contemplated to be immediately issued and they then sell those shares, without disclosure of the profits of the promoters to outside parties, there is no fraud on the corporation* and no ground for complaint by it even though the promoters may derive large profits from the transaction." (Italics ours.)

Later on in its opinion in the *Hays* case, the Court says (p. 21):

> *"Where one is not an original subscriber to stock, but purchases shares from a broker or other vendor of stock, the corporation is not a party to the transaction."* (Italics ours.)

See also:

Mile Wide Copper Co. v. *Piper,* 29 Ariz. 129;
Allenhurst Park Estates v. *Smith,* 101 N. J. Eq. 581;
Hoffman Motor Truck Co. v. *Erickson,* 124 Minn. 279;
Higgins v. *Lansingh,* 154 Ill., 301;
Tompkins v. *Sperry, Jones & Co.,* 96 Md. 560;
Hamilton v. *Hamilton Mammoth Mines,* 110 Or. 546;
Turner v. *Markham,* 155 Cal. 562;
Seymour v. *Spring Forest Cemetery Association,* 144 N. Y. 333;
Wells v. *Northern Trust Co.,* 195 Ill. 288.

The Trial Court, however, disregarding all of these authorities, finds that purchasers from Furlaud & Company, Inc. of the securities so issued by Duquesne Gas Corporation were induced to part with their money in exchange for these securities by reason of alleged misrepresentations and that as a result thereof, somehow—a trust in favor of the corporation resulted (R. 228).

In this connection, he cites the cases of *McKee* v. *Lamon,* 159 U. S. 317, and *Sayer* v. *Wynkoop,* 248 N. Y. 54 (R. 227). An inspection of these cases reveals the fact that in both cases money, admittedly due to the plaintiff, was by his debtor turned over to a third party to be paid to that plaintiff.

In *McKee* v. *Lamon, supra,* a fund was turned over to McKee in trust, requiring him *"to pay over to all parties* who have rendered services heretofore in the prosecution of this claim *the amount due to such persons".* Here, McKee became an express trustee and all that was necessary for the beneficiary to do was to establish his right to participate in the trust fund. The money in controversy was owing to him, and the Court, after fixing the amount due him, declared that he was entitled to receive it from the fund created for the very purpose of paying him and others similarly situated.

In the *Sayer* case, money was due to an insurance company as premiums on its policies and the debtor made payment to his broker with instructions to pay those premiums. Here again the status of creditor existed in the plaintiff who brought suit for these premiums.

In each case, a property right existed in favor of the plaintiff in the fund delivered to the trustee for the very purpose of satisfying his claim.

We do not desire to be understood as contending that it is only where the relation of debtor and creditor exists that money paid to another for the benefit of a third person can be impressed with a trust for the benefit of such third person.

Certainly where a gift is made to such third person in this manner, where a bequest is created for the benefit of a third person, and where in any manner an interest in a trust estate is created for the benefit of a third person, such third person acquires the right to enforce such a trust.

What we do contend is that in order that a trust in favor of a third person can come into existence such third person must have or become entitled to an interest or a property right in the trust fund.

We are unable to see any analogy between the cases cited by the Trial Court and the facts of this case. No person delivered any property or money to Furlaud & Company, Inc., with instructions to pay or deliver the same to Duquesne Gas Corporation.

What happened was that Furlaud & Company, Inc., purchased certain securities from Duquesne Gas Corporation and paid that corporation for them.

It, Furlaud & Company, Inc. in turn sold some of the securities so purchased by it to third parties and the third parties paid it for the securities so purchased.

Next, the Trial Court says that the receiver had the right to bring such suit because he represents not only the corporation but all those having an interest in its property as well. He says:

> "A receivership is for the benefit and protection of all interests, general creditors, secured creditors (bondholders) and stockholders, and it is the

> duty of the court, so far as reasonably possible, to conserve and protect all interests" (R. 229).

Of course we agree with this language in so far as it refers to the property of the corporation which comes into his hands as receiver. As to such property he is a trustee. All of those interested in that property are beneficiaries of the trust, and it is an elementary proposition of law that in the administration of his trust a trustee represents and should protect the interest of all of his *cestui que trustent.*

The Trial Court further states:

> "Although it may be that Duquesne Gas Corporation might not be able, in its own right, to hold Furlaud and Company, Inc., and its masters to accountability for the fraud that was here worked, simple justice requires that the receiver, in his representative capacity, should be able to vindicate the rights of creditors who were victimized" (R. 229).

Just how did the receiver of Duquesne Gas Corporation acquire the right or power to bring suit to vindicate the personal rights of the individuals who became bondholders or noteholders of Duquesne Gas Corporation?

The complainant does not contend that he was appointed Receiver of the personal rights of any individual.

Nor does he contend that any individual assigned his or her rights to him.

Moreover, it does not even appear that any one had rights to be vindicated.

The jurisdictional facts necessary to establish a cause of action on behalf of any of these bondholders or noteholders have neither been alleged nor proven.

The Court merely assumes that some one must have been misled.

Is it not elementary that in order to establish a cause of action for fraud, it is necessary to allege and prove not only (1) that certain representations were made, *but* (2) *that they were false, and* (3) *that they were material? Is it not also essential to show* (4) *that the purchaser relied upon such representations and believed them to be true, and* (5) *acted upon them, and* (6) *that but for such reliance the persons aggrieved would not have entered into the engagement complained of?*

We insist that insofar as the record in this case discloses the facts, no person is shown to have had any rights to be vindicated.

Is it not also true that even if a cause of action did accrue to some one, the person aggrieved had an election of remedies? Had he not the right to go before a Court of Equity to rescind the contract complained of if he so elected? Had he not the right to bring an action at law if he so elected? Does not each person so aggrieved have the separate right to make such election as in his own unrestricted judgment is in his own best interests?

Is not such cause of action personal to each individual aggrieved?

As early as 1885 in the case of Foster v. Seymour, 23 Fed. 65, this question was disposed of.

Wallace, *J.*, in the well considered opinion in that case, states (p. 65):

> "The bill alleges, in substance, that the whole capital stock of the corporation, which was fixed and limited by the certificate of incorporation of the company at 100,000 shares of $100 each, was exchanged by the trustees of the corporation in payment for the purchase of mining property owned by the trustees personally, or some of them,

the value of which did not exceed $100,000 as the trustees knew."

Continuing, he says (p. 66):

"The transaction as alleged was a fraud upon the public. It was equivalent to an overissue of stock by a corporation to its stockholders. It was calculated to lead parties, dealing with the corporation in ignorance of the facts, to believe that it had a paid-up capital stock of $10,000,000, and representing a corporate fund of that amount invested in mining property. By putting out the scrip the trustees represented to the public, who have no means of knowing of the private contracts made between a corporation and its stockholders, that the capital stock had been subscribed for and paid in. It was not a fraud upon stockholders, however, because there were none; nor necessarily upon persons subsequently becoming stockholders, because the stock was full-paid stock, and not liable to any further calls in the hands of those who might purchase it. *Scoville* v. *Thayer*, 105 U. S. 143. *A purchaser of the stock would not be injured by the transaction unless he paid more for it than it was worth; and every purchaser would stand upon the particular circumstances of his purchase.*" (Italics ours.)

In view of the foregoing authorities, we respectfully submit that we can see nothing in the Complaint alleging nor in the evidence establishing any cause of action in favor of Duquesne Gas Corporation, or its Receiver, against any of the Defendants.

POINT IV

UNDER THE FACTS OF THIS CASE THE PLAINTIFF IN HIS CAPACITY OF RECEIVER HAS NO GREATER RIGHTS OR POWERS THAN THE CORPORATION ITSELF WOULD HAVE.

Petitioner contends, under his fourth point, that the plaintiff in his capacity as receiver and standing in the right of the creditors has the right to disaffirm the acts of the corporation.

He refers to a number of cases where fraud was perpetrated upon a corporation and upon its stockholders by a Board of Directors who were under the control of some of its stockholders.

In all of these cases, at the time of the transaction complained of, there were innocent stockholders or creditors in existence who had not consented to the improper conduct of the Board (as in the case of *Leach* v. *Grant,* 54 F. (2) 731, *Davis* v. *Las Ovas, supra,* and *Casey* v. *Cavaroc,* 96 U. S. 467). The law upon this subject has always been well settled and it is to the effect that the directors of a corporation are trustees for the corporation and as such are trustees for its stockholders and creditors. Any act of theirs in violation of their obligation as trustees is, of course, actionable. We have shown under the third point of this brief that under the facts of this case no such relationship existed or could have existed as a matter of law.

See

Ball v. *Breed, supra;*
Ball v. *Chapman,* 1 F. (2d), 895;
South Penn Collieries Co. v. *Sproul,* 52 F. (2d) 557;
Tompkins v. *Sperry, Jones & Co.,* 96 Md. 560.

Moreover, as we have shown under the first and second points of this brief, there is no allegation in the complaint in this case that charges that any wrong was practiced on any one.

POINT V

THE CONTENTION OF THE PETITIONER THAT THE CORPORATION WAS POWERLESS TO RENDER ITSELF INSOLVENT BY A SURRENDER TO THE DEFENDANTS OF ITS RIGHT TO HOLD THEM ACCOUNTABLE TO IT FOR THE PROCEEDS WHICH CAME INTO THE HANDS OF DEFENDANTS FROM THE SALE OF THE SECURITIES OF THE CORPORATION, IS NOT ONLY NOT WITHIN THE ISSUES PRESENTED BY THE COMPLAINT, BUT UNDER THE FACTS OF THIS CASE IS UNSOUND.

We feel constrained to again call the Court's attention to the fact that there is no allegation in the complaint which raises the issue with which Point V of the petitioner's brief is concerned, even if it were sound. We have discussed this question under Points I and II.

Ever since the decision of this Court in the *Lewisohn* case, every conceivable argument has been advanced to evade its effect. The case of *Davis* v. *Las Ovas, supra,* is in no sense and in no part in conflict with the decision in the *Lewisohn* case.

In the *Lewisohn* case it was held that where, as the result of transactions between promoters and a corporation, the promoters acquired *all of the stock of such corporation* no disclosures of the cost of the property transferred were

required because the promoters were merely selling to themselves and as purchasers knew all of the facts involved in the transaction.

The *Las Ovas* case holds that where at the time of the transaction complained of the promoters *did not acquire or have all of the existing issued stock of the corporation,* or, in other words, if there were at that very time innocent interested stockholders of the corporation in existence, the obligation to make full disclosures did exist. The *Las Ovas* case has been used as the basis for innumerable arguments to the effect that parties who have contracted to become stockholders and bondholders and have actually advanced or agreed to advance money to the promoters in exchange for securities to be sold to them by such promoters if, as and when issued, became by reason of their contractual relationship equitable parties in interest. The action of this Court in refusing to grant a writ of certiorari in the case of *Ball* v. *Breed, supra,* in the application for which this very question was so vigorously urged, seems to us to dispose of that question.

The precise question here involved has been decided in a number of cases. We will content ourselves with quoting from two.

In *Wells* v. *Northern Trust Co.,* 195 Ill. 288, the Construction Company to whom the bonds and stock were issued originally received $15,000,000, half in stock and half in bonds of the company, but the cost of building and equipping the entire road was $7,728,102.94. This company was insolvent. The Court said (p. 296):

> "It is not shown that there were then any stockholders or creditors who were injured by this action against their consent. All then interested in the

> company, having assented to the contract and its modifications, and to the mortgage and the issuing of the bonds, the company and the successors in interest of the then stockholders are estopped from setting up the inequality or oppressiveness of the construction company's contract."

In the case of *Seymour* v. *Spring Forest Cemetery Association,* 144 N. Y. 333, the Court, after discussing this very question, uses the following language (p. 340):

> "Evidence was given to show that the land conveyed was not worth the sum secured, but that is a totally immaterial fact. Whatever the price, it wronged no one and could wrong no one, and accomplished nothing except to fix a primary limit to the anticipated profits."

POINT VI

THE QUESTION PRESENTED BY PETITIONER UNDER POINT VI OF HIS BRIEF, HAVING BEEN RAISED FOR THE FIRST TIME UPON THE SECOND ARGUMENT OF THE APPEAL OF THIS CASE, COULD NOT IN ANY EVENT BE CONSIDERED BECAUSE

(1) There is no allegation in the complaint under which this issue, if sound, could have been raised;

(2) It is in direct conflict with the theory upon which the case was tried in the lower court.

Under Point VI of the petitioner's brief he contends that all of the securities issued by Duquesne Gas Corpo-

ration were void under the Pennsylvania Constitution; that the defendants at no time were in the position of stockholders, bondholders or noteholders of the corporation.

As a matter of fact, none of the defendants in this case except Kingston Corporation ever acquired a single share of stock, a bond or a note from Duquesne Gas Corporation, so as to them the question if otherwise sound could not be asserted.

1.

We will not here discuss the soundness of the proposition advanced by petitioner beyond saying that one of the leading cases in America following the rule laid down in the *Lewisohn* case, is the case of *South Penn Collieries Co.* v. *Sproul,* 52 F. (2nd) 557, which involves a Pennsylvania corporation.

We will content ourselves here with calling the attention of this Court to the fact that this question was first presented on the second argument before the Court of Appeals. Nor shall we here make extensive reference to the fact that there is no allegation in the complaint under which this theory could have been considered by the lower court or by the Court of Appeals.

Counsel for petitioner has so often asserted in his briefs and arguments that the fiduciary relationship which he claimed between some of the defendants and Duquesne Gas Corporation arose out of the representations made by them or some of them, or by corporations dominated by some of them, to the purchasers of these securities that we were constrained to believe that that was the theory upon which he was relying.

2.

Petitioner's statement in his first brief as respondent in the Court of Appeals in which he states as the basis of the judgment entered in favor of the complainant, is as follows:

> "That when a banker or promoter assures the purchasers of corporate bonds that the proceeds of sale are to be turned over to the corporation or used for its benefit, he is bound to make that assurance good; that when the bondholders contribute money on the face of such assurances a trust relation arises of which the corporation is the beneficiary; that the corporation has an enforceable right to receive the benefit of the proceeds of the bonds. This is a property right and it cannot be given away to the prejudice of creditors, even with the consent of all the stockholders. If the right is given away, or, to put it more bluntly, if the proceeds of the bonds are converted by the promoters to the prejudice of the creditors of the corporation, the receiver of the corporation can maintain an action to recover the moneys so converted, though the unanimous consent of the stockholders might have barred an action by the corporation."

It must be remembered that the only representations that he alleges were made were to the effect that the securities were or are issued in connection with the acquisition of property and to provide working capital for the corporation. He does not even allege that that representation was not true, but true or false, he insisted that as a result of that statement the relation of trustee was impressed upon Furlaud & Company, Inc. He nowhere alleges that

the securities issued were in excess of the value of the property, but he does show the cost of the property.

From the beginning of the trial petitioner has absolutely disregarded the allegations in his complaint. He has treated it as a mere scrap of paper having no function but to mislead defendants as to the basis of his claim.

In the lower court he succeeded in introducing evidence indicating that the value of the properties, though admittedly in excess of their cost, was much less than the price for which they were appraised. We think we have shown under Point II of our Brief that the admission of this testimony constituted reversible error. We most strenuously objected to it and exceptions were taken and allowed.

But even then the petitioner never advanced any other theory than that hereinbefore set out as representing his theory in this case.

If there be any basis for the rule that in an appellate court a party is bound by the construction he puts upon his pleadings in the lower court and upon the theory of fact upon which he there submitted his cause or defense, how can the defendant upon his second brief and argument before an appellate court for the first time present an entirely new theory not suggested in his complaint and never urged or relied upon by him before?

In *Texas & P. R. Co.* v. *Abilene Cotton Oil Co.*, 204 U. S. 426, this Court very definitely holds that an intermediate Appellate Court cannot consider a theory different from that upon which a case had been tried in the lower court.

In *Rees* v. *Lombard*, 21 F. (2d) 276, the Circuit Court of Appeals of the Ninth Circuit says (277):

> "* * * The rule is well settled that, in an appellate court, a party is bound by the construction he put

> upon his pleading in the lower court, and the theory of fact upon which he there submitted his cause or defense."

In *Ehmen* v. *City of Gothenburg, Neb.* 200 Fed. 564, at 566, the Circuit Court of Appeals for the Eighth Circuit says:

> "It would be manifestly unjust, when a case has been narrowed to an issue by pleadings and trial, and a bill of exceptions submitted and allowed to present the ruling of the trial court, for an appellate court to entertain a new and different question on the merits."

See also:

Albany Perforated Wrapping Paper Co. v. *John Hoberg Co.*, 109 Fed. 589;
Lesser Cotton Co. v. *St. Louis I. M. & S. Ry. Co.*, 114 Fed. 133;
Van Norden v. *Chas. R. McCormick Lumber Co.*, 17 F. (2d) 568;
Roof v. *Rule*, 348 Ill. 370;
Svenson v. *Svenson*, 178 N. Y. 54.

The Supreme Court of the United States in reversing the decision of the Circuit Court of Appeals for the Second Circuit on the former appeal in this case (*McCandless* v. *Furlaud*, 79 L. Ed. 32) most emphatically recognized this doctrine. Although in that case the question of the title of plaintiff was put in issue by what this court held to be a constructive denial this Court held that that question could not for the first time be raised in an Appellate Court.

POINT VII

THE TRIAL COURT PROPERLY DISMISSED THE COMPLAINT AS TO THE DEFENDANTS BYRON CORPORATION AND CHAUCER CORPORATION.

Byron Corporation and Chaucer Corporation had dealings solely in the stock of the Duquesne Gas Corporation.

The Trial Court dismissed the complaint as to these two defendants on the authority of *Old Dominion Copper Co.* v. *Lewisohn,* 210 U. S. 206 (R. 232).

Byron Corporation and Chaucer Corporation were organized in May of 1930.

The stockholders of Byron Corporation were Eleanor Mortimer Furlaud and Kipling Corporation who owned 10,000 and 30,000 shares of its stock respectively (R. 109). Eleanor M. Furlaud is the wife of the defendant Maxime H. Furlaud (R. 103). It does not appear who were the stockholders of Kipling Corporation.

Chaucer Corporation was organized at about the same time. The stockholders of that corporation were Elsie Reuter and Virgil Corporation who owned 10,000 and 30,000 shares of its capital stock respectively (R. 112).

Elsie Reuter is the wife of Carlos Reuter (R. 103). It does not appear who were the stockholders of Virgil Corporation.

Byron Corporation and Chaucer Corporation had acquired options to purchase from Kipling Corporation 255,000 shares each of the common capital stock of Duquesne Gas Corporation for 50 cents a share (R. 101-102).

Subsequently and on or about the 27th day of May, 1930 these options were exercised and notes were executed by both these corporations to Kingston Corporation in

the sum of $127,500 each payable with interest at 6 per cent. These notes were thereafter paid and Kingston Corporation received from Byron and Chaucer Corporations approximately $265,000 in payment for the stock (R. 102, 125).

On May 29, 1930 an agreement was entered into between Chaucer Corporation, Byron Corporation and John J. Bergen (R. 97, 200-201). Under this agreement Mr. Bergen obtained an option to purchase all or any part of 100,000 shares of the common stock of Duquesne Gas Corporation at $10.00 per share, a further option to purchase all or any part of an additional 150,000 shares at $12½ per share and a further option to purchase 50,000 shares at $14 per share. Subsequently Mr. Bergen purchased under this option agreement 42,500 shares from Byron Corporation and paid therefor the sum of $425,000 (R. 96).

There is no testimony in the record which indicates that any other shares were sold to Bergen or that any other sums of money were received by Byron Corporation or Chaucer Corporation from him or from any one else.

On the basis of these facts the Court properly dismissed the complaint as to Byron and Chaucer Corporations.

There is no testimony of any kind in any way connecting these corporations with any of the transactions complained of by petitioner. It is in evidence that Mrs. Furlaud owned 25 per cent. of the stock of Byron Corporation and that Byron Corporation bought and paid for 255,000 shares of Duquesne Gas Corporation stock. Three-quarters of the stock was owned by another corporation concerning the ownership of which no evidence was offered. Elsie Reuter occupied the same position towards the Chaucer Corporation. There is no evidence which in any manner connects either Mrs. Furlaud or Mrs. Reuter with any of the trans-

actions referred to herein or that they knew of any of the facts complained of by the petitioner.

The corporation in which each of them was interested purchased this stock at a price in excess of any value placed upon it by the petitioner. Petitioner contends that the Duquesne Gas Corporation was insolvent and that its stock had no value of any kind. The stock had no par value and at most represented the equity in the properties of Duquesne Gas Corporation in excess of its bond and note indebtedness.

We respectfully submit that not only did the Court properly dismiss the complaint as to these corporations for the reasons given by him but that in addition there was no evidence of any kind offered to the effect that these corporations were not perfectly innocent purchasers for value of the securities purchased by them.

POINT VIII

THE DEFENDANT FURLAUD IS NOT PERSONALLY LIABLE IN THIS CASE IN ANY EVENT.

Under Point VII of his brief, the petitioner contends that "the defendant Furlaud is personally accountable for the fraudulent misappropriation."

The Court of Appeals held on the basis of undisputed evidence that:

> "Maxime H. Furlaud had no relation to these transactions other than as an officer and director of Furlaud & Co. Inc., and his personal activity in carrying on the negotiations and transactions. He did not participate in the alleged fraudulent appraisal or receive personally any of the monies paid to Furlaud & Co. Inc." (R. 267).

It nowhere appears in the record that Furlaud personally received any of the funds paid to Furlaud & Co. Inc.

The petitioner relies on the case of *Anderson* v. *Daley*, 38 App. Div. 505, which is a case involving the actual misappropriation of trust funds that came into the possession of a corporation. The President of the corporation was a party to the misappropriation and he was held liable as a trustee *de son tort*. However, as we have shown before, no trust funds ever came into the possession of Furlaud & Company, Inc. It merely sold some bonds and notes to various people who purchased them.

POINT IX

THE COMPLAINT AFFIRMATIVELY SHOWS THAT COMPLAINANT HAD NO TITLE TO ANY CAUSE OF ACTION THAT COULD HAVE BEEN ASSERTED BY DUQUESNE GAS CORPORATION.

The attention of the Court is here for the first time called to the fact that:

In paragraph "Second" of complainant's amended complaint (R. 4) he alleges that he is a resident and citizen of the Commonwealth of Pennsylvania and that Duquesne Gas Corporation is a corporate citizen of the Commonwealth of Pennsylvania, and,

In paragraph "Fourth" (R. 4-5) he alleges that upon petition of complainant filed in the United States District Court for the Southern District of New York an order was duly made appointing such complainant ancillary receiver of Duquesne Gas Corporation.

In its decision in the case of *McCandless* v. *Furlaud*, 79 L. Ed. 32, this Court said, referring to the case of *Booth* v. *Clark*, 17 How. 322 (p. 36):

> "There, the foreign equity receiver suing in the federal court of another State failed because, having no title to the assets within the district, he was without a cause of action.. * * * For that reason, a bill in the federal court for southern New York brought by the primary receiver, alleged to have been duly appointed in Pennsylvania and authorized to bring this suit, would have been bad on demurrer. But this bill by the ancillary receiver, which alleges that he had been duly appointed by the federal court for New York and authorized to bring the suit, would have been good on demurrer."

Ordinarily we would assume that the decision of this Court in the case of *McCandless* v. *Furlaud, supra,* disposes not only of any issues that were presented but of any that might have been.

However, this Court in the case of *Mitchell* v. *Maurer*, 79 L. Ed. 149, decided subsequent to the decision in the *McCandless* case, *supra,* held that the appointment of the Receiver in that case was void for lack of diversity of citizenship, although the question was not raised either in the lower court or in this Court. Mr. Justice Brandeis, speaking for the Court, says (p. 153):

> "Unlike an objection to venue, lack of federal jurisdiction cannot be waived or be overcome by an agreement of the parties. An appellate court must satisfy itself not only of its own jurisdiction, but also of that of the lower courts in a cause under review. *Mansfield, C. & L. M. R. Co.* v. *Swan*, 111 U. S. 379, 382, 28 L. ed. 462, 463, 4 S. Ct. 510. Hence,

> the failure of the Insurance Commissioner to claim, in his petition for certiorari, that the order of the District Court was void for lack of federal jurisdiction of the suit, and his failure otherwise to call to the attention of this Court the lack of diversity of citizenship are immaterial."

In view of this decision we feel it our duty to our clients as well as to this Court to call attention to the fact that it affirmatively appears from the pleading in this case that the appointment of complainant as ancillary receiver was void. The complaint shows that the appointment was made on the petition of a citizen of the Commonwealth of Pennsylvania to have an ancillary receiver of the Duquesne Gas Corporation, also a corporate citizen of the State of Pennsylvania, appointed. That the Duquesne Gas Corporation was a necessary party to any proceeding to have a receiver of its assets appointed seems too clear for argument.

In view of the fact that in its former decision this Court distinguished a case where a defect in petitioner's title appears upon the face of the complaint from one in which it is merely constructively raised by answer, and in the *Maurer* case expressly held that where the lack of federal jurisdiction consisted of the lack of diversity of citizenship the matter was one that not only could not be waived but which the Court would of its own motion investigate, we feel constrained to call this Court's attention to these allegations in the complaint, but unless requested so to do shall not further discuss the question involved.

CONCLUSION

The judgment of the United States Circuit Court of Appeals for the Second Circuit, filed March 11, 1935, should be affirmed.

Respectfully submitted,

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IRA W. HIRSHFIELD,
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Of Counsel.

October, 1935.

APPENDIX

In the appendix to his brief the plaintiff discusses the doctrine enunciated in the cases of *Old Dominion Copper Mining and Smelting Company* v. *Lewisohn,* 210 U. S. 206, and that enunciated in *Old Dominion Copper Mining and Smelting Company* v. *Bigelow,* 203 Mass. 159.

It is true that upon the question which is involved in the decision of the *Lewisohn* case there are two lines of authorities in this country. One is known as the "Federal rule" and the other as the "Massachusetts rule".

As a corollary to the rule adopted in the *Lewisohn* case, it was held in *Davis* v. *Las Ovas,* 227 U. S. 80, that where at the time of the transaction between promoters and a corporation, the promoters were *not the owners of all of the stock of the corporation,* there was a duty of disclosure to innocent existing stockholders. There is not the slightest conflict between these decisions. The decision in the latter case follows obviously and naturally from the decision in the former.

The Massachusetts rule was, by the case of *Hays* v. *The Georgian,* 280 Mass. 10, so clarified that the Massachusetts rule now is that where at the time of the transaction complained of the promoters *are the original subscribers to the entire capital stock contemplated to be immediately issued,* the corporation did not and could not have any cause of action against them.

Since in this case there can be no question whatever of the fact *Furlaud & Company, Inc. and Kingston Corporation were the original subscribers to the entire capital stock contemplated to be immediately issued,* we do not think that the discussion is pertinent.

Moreover, we do not think that the analysis of the cases made in petitioner's Appendix is justified. For instance, petitioner refers to such cases as *Yeiser* v. *U. S. Board & Paper Co.*, 107 Fed. 340, *New Sombrero Phosphate Co.* v. *Erlanger*, L. R. 5 Ch. Div. 73, 46 L. J. Ch. N. S. 425, 36 L. T. N. S. 222, 25 Week. Rp. 436, and cases like *Tilden* v. *Barber*, 268 Fed. 587 and *American Shipbuilding Co.* v. *Commonwealth S. S. Co.*, 215 Fed. 296 as cases based on the theory that the promoters were in the position of trustees to future stockholders of the corporation.

An examination of these cases shows that the decision of the Court was based upon a complete realization of the distinction first announced by this court in the cases of *Old Dominion Copper Co.* v. *Lewisohn* and *Davis* v. *Las Ovas.* For instance, in the case of *Tilden* v. *Barber*, the court after holding that Barber was not a trustee to the millers for the reasons set out, spoke of the subscriptions made by the public and uses this language, (p. 602):

> "To such of them as had subscribed for the stock of this company, *and had paid a portion of the amount due on their subscription at the time Barber's proposal was accepted by his dummy directors* (and there were a number of such subscribers), he owed the duty of making a full disclosure, or, failing in that, to make it to an independent and competent board of directors of the company when formed" (Italics ours).

In the case of *American Shipbuilding Co.* v. *Commonwealth S. S. Co.* speaking of the facts in that case, the Court said (p. 299):

> "What they did do was to proceed exactly as planned, organize the corporation, exchange their

> subscription rights for capital stock, and then, as a corporation, take over and complete the contract which their agent had made."

Here again there were actual interested innocent stockholders at the time the transaction was completed.

Petitioner refers to the case of *Humble Oil Co.* v. *Campbell*, 69 F. (2d) 667. That is a case of a trustee selling the title to property belonging to others and not accounting to his *cestui que trust* for the proceeds of the sale, and the Court expressly says, in speaking of the facts of that case and of the Federal rule (p. 670):

> "It is not necessary to determine under which line of decisions this case falls. It is maintainable upon the broad powers of a trustee to follow and gather in trust property, and hold to an account those who have taken it."

Nor can we understand petitioner's statement that in cases like *Ball* v. *Breed*, 294 Fed. 227, *South Penn Collieries Company* v. *Sproul*, 52 F. (2d) 557 and *Johnson* v. *Louisville Trust Co.*, 293 Fed. 857, the decisions were ultimately based upon the fact that no fraud was actually practiced by the promoters. If he means that no fraud was actually practiced by the promoters on the corporation, because they were the corporation, that they sold to themselves and could not practice fraud upon themselves, of course we agree with him, but certainly in the case of *Ball* v. *Breed* a profit of $1,100,000 was taken by the bankers and it was not disclosed to their associates in the syndicate whose money they used in organizing the corporation.

In the *South Penn Collieries* case, Sproul and Jackson acquired properties for $384,000 which they resold to the South Penn Collieries Co. for $700,000, thus making a net

profit of $316,000 in the first transaction, and in the second transaction made an additional profit of $217,666.67.

We further regret to say that we cannot construe many of the cases cited by counsel for petitioner in his Appendix as standing for the proposition claimed for them.

Of the cases cited by the petitioner three others seem to have no possible application to the question.

In *Downey* v. *Byrd,* 171 Ga. 532, three stockholders sued the promoters to recover the purchase price of stock issued to them by a corporation on the ground that the defendant promoters had by fraud and deceit caused them to purchase stock. This case obviously does not involve a question of promoters' profits, but a simple case of fraud and deceit.

In *Land Co.* v. *Lewis,* 101 Me. 78, a corporation sought an adjudication that the defendants were holding the legal title to land as trustees for the corporation and to compel a conveyance of the property to the company. The defendants, who were its officers, had diverted the company's monies and had purchased property with such funds. These funds were traced into land purchased by the defendants. The corporation was held entitled to impress a trust upon these lands to the extent of its interest therein.

In *American Forging Co.* v. *Wiley,* 206 Mich. 664, an action was brought by the corporation to compel a promoter to perform a contract entered into by him for the benefit of the corporation and which he had failed to perform. This court does state that it adopts the Massachusetts rule, but its application to the facts is difficult to understand.

In quite a number of the cases cited by Petitioner in the Appendix to his brief, the Federal rule as announced in *Davis* v. *Las Ovas* is followed. The decisions in those cases are not in conflict with the case of *Old Dominion Copper*

Co. v. *Lewisohn*. Under the facts as disclosed, the *Lewisohn* case does not apply.

As we have hereinbefore stated, there are a number of state court cases which have adopted the Massachusetts rule but we think that far the greater number of state courts have adopted the federal doctrine.

In 1 Fletcher on Corporations (Perm. Ed. 1931) at page 648, the author in discussing the *Lewisohn* and *Bigelow* rules states that:

> "The marked tendency of the State Courts has been to follow the United States Supreme Court."

Ehrich, in his work on Promoters at page 265, says:

> "If one may be permitted to express an opinion on the merits of the question upon which the highest courts in the land disagree, it is, after much hesitation, suggested that the decision of the Supreme Court of the United States is on the whole to be preferred."

The following authorities have adopted the rule as laid down in the *Lewisohn* case:

Hughes v. *Cadena de Cobre Min. Co.*, 13 Ariz. 52;
Garretson v. *Pacific Crude Oil Co.*, 146 Calif. 184;
Lilylands Canal & Reservoir Co. v. *Wood*, 56 Colo. 130;
Soule v. *Kunkle*, 71 Colo. 221;
Higgins v. *Lansingh*, 154 Ill. 301;
Wells v. *Northern Trust Co.*, 195 Ill. 288;
St. Louis F. S. & W. R. Co. v. *Tiernan*, 37 Kan. 606; 633;

Hoffman Motor Truck Co. v. *Erickson*, 124 Minn. 279;
American Barley Co. v. *McCourtie*, 150 Minn. 460;
Tompkins v. *Sperry, Jones & Co.*, 96 Md. 560;
Seymour v. *Spring Forest Cemetery Association*, 144 N. Y. 333;
Blum v. *Whitney*, 185 N. Y. 232;
Roberson v. *Draney*, 53 Utah 263;
Inland Nursery & Floral Co. v. *Rice*, 57 Wash. 67;
Metcalfe v. *Mental Science Ind. Ass'n*, 127 Wash. 50, 56 *et seq.*

We do not here cite many cases like that of *Hays* v. *The Georgian*, 280 Mass. 10, because they do not completely adopt the rule laid down in the *Lewisohn* case, but as an evidence of the trend of the courts we call attention to the fact that even Massachusetts through its highest court has held that if at the time of the transaction complained of "the promoters and those acting in concert with them are the original subscribers to the entire capital stock *contemplated to be immediately issued* and they then sell those shares, without disclosure of the profits of the promoters, to outside parties, there is no fraud on the corporation and no ground for complaint by it even though promoters may derive large profits from the transaction. That principle seems to prevail generally." (Italics ours.)

However, we feel that any discussion of the advisability of following the *Bigelow* case in the determination of the issues before this Court is hardly pertinent, first because this Court decided both the *Lewisohn* case and the *Las Ovas* case and we must assume that those cases announce the law

on this subject, and second, because even under the Massachusetts rule plaintiff could not recover under the facts of this case, for the reason that at the time of the transaction complained of Furlaud & Company, Inc. and Kingston Corporation became original subscribers to the entire securities contemplated to be immediately issued, and if they then sold those securities *without disclosure of their profits to outside parties* there could be no fraud upon the corporation, no ground for complaint by it even though they may have derived large profits from the transaction.

We have gone to this length in discussing the appendix in our opponent's brief in order not to create the impression that we concede that the cases referred to by him stand for the propositions suggested.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of Duquesne Gas Corporation,

Complainant,

against

MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION, and CHAUCER CORPORATION,

Defendants.

PETITION FOR REHEARING ON BEHALF OF MAXIME H. FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION AND CHAUCER CORPORATION, DEFENDANTS BELOW.

LOUIS B. EPPSTEIN,
Counsel for Petitioners.

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To the Honorable Charles E. Hughes, the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The above-named defendants, Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, present this, their petition for a rehearing of the above-entitled cause.

Jurisdiction.

The petition for certiorari in this cause was filed on April 18, 1935, and certiorari was granted on May 13, 1935. This Court rendered its decision on November 11, 1935 reversing the judgment of the United States Circuit Court of Appeals for the Second Circuit and modifying its judgment in other respects.

This petition is filed within less than twenty-five days thereafter under Rule 33 of the General Rules of the United States Supreme Court.

Reasons for Petition for Re-hearing.

The petitioners contend:

I.

That in its consideration of the admissibility of the testimony concerning overvaluation of the property conveyed to Duquesne Gas Corporation and concerning misrepresentations of value made to purchasers of securities of Duquesne Gas Corporation by these promoters, this Court in its majority opinion inadvertently overlooks several important factors.

A. The Court says:

> *"The complaint was based upon the theory that the promoters had been guilty of unconscionable conduct."* (Italics ours.)

There were no facts alleged in the complaint from which any unconscionable conduct could be inferred.

The theory upon which the complaint was based was that every transaction between a promoter and a corporation organized by him, in which the promoter makes a profit as a result of the sale of the securities received by him from the corporation in exchange for property transferred to it by him, is unconscionable.

This, of course, is unsound.

The unconscionable conduct upon which the majority opinion of this Court was based consisted of the claim that an appraisal of the properties conveyed to Duquesne Gas Corporation grossly overvalued the properties so conveyed, and that the representations made by the promoters to the public upon the offering of these securities was to the effect that the appraised value represented the fair market value of these securities.

The complaint did not allege any of these facts, and it is our contention that the evidence tending to establish them was improperly admitted.

The facts actually alleged were that Duquesne Gas Corporation was organized by the promoters who owned all of its stock; that the promoters had acquired options on oil and gas properties in Pennsylvania at a cost of $2,500,000 prior to the organization of the corporation; that prior to actually exercising their options the promoters secured subscriptions from the public for part or all of the bonds and notes to be issued by the corporation; that the promoters thereafter caused the corporation to acquire the properties from them at a price largely in excess of $2,500,000 and issued its bonds and notes to the promoters in payment and that as a result of disposing of the bonds and notes so acquired by the promoters they made a large profit out of the transaction.

There is certainly nothing improper or unconscionable necessarily growing out of that statement of facts. If it be assumed that the property optioned to the promoters had greatly enhanced in value or was worth more than was paid for it, and that the par or stated value of the securities issued was less than the fair value of the property exchanged, no one could justly criticize the transaction.

Certainly, under that state of facts no cause of action could possibly accrue either to the corporation which acquired the properties or to the public who acquired the securities.

Something more than appears in this complaint must be shown to establish a cause of action.

Under the law as it existed prior to this decision:

If the action were one to recover secret profits, it was necessary to show that the promoters were not the sole owners of the stock of the corporation at the time of the transaction and that they practiced a fraud on the other interested parties.

If the action were one brought by a purchaser of the securities, allegations of fraud and misrepresentation of some character were required.

Under the new theory established by this opinion it should be necessary to make allegations in the complaint which would bring the case within such theory.

What we here contend is that this complaint contains no such allegations.

There is no allegation in the complaint as to what was the value on April 7, 1930, the closing date, of the property transferred to Duquesne Gas Corporation.

Nor is there any allegation in this complaint to the effect that any misrepresentations as to the value of the property

acquired by Duquesne Gas Corporation were made to any one. The complaint does not allege that there was an appraisal made or that the appraisal overvalued the property referred to therein or that any such facts were communicated to any one.

There was no allegation in the complaint to the effect that the corporation was either rendered insolvent or that its capital was impaired by these transactions.

The majority opinion of this Court is based entirely upon the assumption that these facts were sufficiently established. That there was in the record evidence tending to establish these facts must be conceded but it was the admission of this very testimony that was so strenuously objected to and concerning which exceptions were not only requested by the defendant but stipulated to by counsel for the plaintiff and formally granted by the Trial Court.

What we here call to the attention of this Court is that testimony was introduced upon the trial of this case (over the most strenuous objections and exceptions of these defendants) tending to show that the value of the property acquired by Duquesne Gas Corporation was less than that at which it had been appraised and that fraudulent misrepresentations had been made to the public concerning its value under a complaint that did not allege any of these facts. The majority decision of this Court is based solely upon this evidence.

Nor is there anything in the laws of Pennsylvania which could be invoked by the plaintiff under this complaint.

Under the Constitution of the Commonwealth of Pennsylvania, securities issued in excess of the *value* of the property conveyed to a corporation in exchange therefor are, under certain circumstances, declared to be void. This

certainly cannot mean that, if the securities were conveyed to the corporation in excess of their cost to the transferor but not in excess of their then fair market value, such securities would be void.

That oil and gas and mining properties rapidly increase and decrease in value is so well known as to be referred to in many decisions upon this subject.

B. The opinion next comments upon our right here to rely upon the exceptions taken in the lower court, notwithstanding the fact that plaintiff three times stipulated that we should have an exception to the entire line of testimony and that the Trial Court, upon the introduction of the very last testimony upon this subject, formally stated in his last ruling upon this subject that the defendants "may have an exception to this line of testimony" (R. 113).

The opinion says:

> *"To this it may be added that the trial judge received the testimony provisionally and subject to a motion to strike out when all the evidence was in. The motion was not made."* (Italics ours.)

We respectfully insist that this Court has inadvertently overlooked certain very vital facts in connection with the admission of this testimony. It is true that after the first objection to the admissibility of this line of testimony was made, and an exception duly taken, some discussion occurred and the Trial Judge stated that he would take the testimony for the present but would later entertain a motion to strike it out (R. 60).

But as the case proceeded the defendants so often and so persistently objected, claimed surprise, and told the Court

that they were not prepared to proceed with the trial upon the theory presented by this line of inquiry (R. 57-60, 61, 62, 63, 109, 113) that, finally, the plaintiff on three different occasions stipulated in open court that the defendants should be held to have an exception to this entire line of testimony (R. 53, 54, 63).

Moreover, at the very end of plaintiff's case, in fact when the very last question on this subject asked of any witness was put to Charles C. Nuss concerning the value of certain tracts included in the appraisal, a final objection was made, whereupon the Court, after granting an exception to the admission of that testimony, said:

> "Yes, you may have an exception to this line of testimony" (R. 113).

Under these circumstances was a motion to strike out required of these defendants?

We do not think that a motion to strike out testimony admitted over objection, argument and exception such as took place in this case has ever been required. Of course, where testimony has been received provisionally subject to a motion to strike it out at the end of the trial and *where no exception has been taken to the ruling of the court at the time of its admission,* failure to make such motion leaves the testimony in the case. The reason for this rule is obvious, particularly if the testimony so admitted involved issues that could be cured by amendment of the complaint without prejudice to the parties.

In this case, however, the defendants objected to the introduction of testimony along these lines so persistently as to cause counsel for defendants to feel that further argument or persistence on this subject would simply result in

annoyance to the Court. This was the more true because counsel for plaintiff had, as we have shown, three times stipulated that defendants should have an exception to this entire line of testimony, but finally at the very end of plaintiff's case defendant again called the attention of the Court to its position on this subject and the Court stated:

> "Yes, you may have an exception to this line of testimony" (R. 113).

This was the final ruling of the Court upon this subject, and, we respectfully insist, was intended by the learned Trial Court to protect the defendants' rights in this respect and was so accepted by the defendants.

As stated by Judge Sanborn in *Salt Lake City* vs. *Smith,* 104 Fed. 457, at page 470:

> "When a question has once been fairly presented to the trial Court, argued, and decided, and an exception to the ruling has been recorded, it is neither desirable nor seemly for counsel to continually repeat their objections to the same class of testimony, and their exceptions to the same ruling which the court has advisedly made as a guide for the conduct of the trial. Counsel for the city lost nothing by their failure to annoy the Court by repeating an objection which it had carefully considered and overruled."

In *Grand Trunk Pac. Ry. Co.* v. *Tollard* (C. C. A. 8th) 286 Fed. 676, the Court says (p. 678):

> "Nor is it necessary after an objection to the admission of incompetent testimony has been erroneously overruled, to move to strike that testimony, no more so than to repeat objections to a class of evidence, after an objection has once been overruled."

In *Walrath* v. *Hanover Fire Ins. Co.*, 216 N. Y. 220, the Court says at page 225:

> "At the close of the entire evidence the court permitted the plaintiff, under the proper objection and exception of the defendant, to insert in the complaint, as an amendment, allegations to the effect that the defendant agreed to deliver the policy of insurance and had failed and neglected to perform that agreement. The defendant, as we have stated, objected throughout the trial to the admissability of the evidence in proof that the defendant made a parol agreement to insure the plaintiff and violated it. The complaint could be amended only at a time which would give the defendant a right and opportunity to meet by proof the allegations made against it."

See also *Northam* v. *Dutchess Co. Mut. Ins. Co.*, 177 N. Y. 73.

> *In this connection we desire to call attention to the fact that there was never any motion made by the plaintiff to conform his pleadings to the proof.*

He stood upon his pleadings from the beginning. He filed a complaint and then an amended complaint. Nor was he ambushed into this situation. Before any answer was filed, a motion was made to require him to make a further and better statement of his cause of action (R. 13). He refused to do this. He elected to stand upon his complaint then. He elects to stand upon his complaint now.

Counsel for complainant has never questioned the fact that defendants had a valid exception to the action of the Court in admitting this testimony. In his argument in the lower court and in his argument before this court he con-

tended that this testimony was admissible under the complaint as framed. He contended, in effect, that having alleged that the defendants were promoters, therefore trustees, he was at liberty to introduce any testimony showing or tending to show a violation of their duties as trustees even if the ultimate facts showing such violations were not alleged. He contended that the allegation in the complaint concerning the purposes of the issue, whether true or false, created a trust relationship.

We respectfully insist that the orderly administration of justice and the traditions of this court require much more of a complaint. This court has always held that a complaint must contain allegations of the ultimate facts to be relied upon, that it is not sufficient to allege generally that the acts of the defendant were unconscionable or merely that a trustee violated his duty as such. Such allegations are mere conclusions of law and if unsupported by allegations of facts, raise no issue. At least the ultimate facts to be relied upon to establish a charge of unconscionable conduct or a violation of duty must be alleged.

In *Fogg* v. *Blair*, 139 U. S. 118, at page 127, Mr. Justice Harlan, speaking for this Court, says:

> "As he impugned the good faith of the transaction between the company and the contractors, it was incumbent upon him to state the essential, ultimate facts upon which his cause of action rested, and not content himself with charging, generally, that what was done was 'colorable,' a 'fraud,' a 'breach of trust,' and a 'scheme' by which Blair and Taylor were to get the stock without paying for it. These are allegations of legal conclusions merely, which a demurrer does not admit. * * * It is consistent with the allegations of the bill that the stock

> was absolutely without value when issued to Blair and up to the time when the railroad and all the property appurtenant thereto was sold under the decree of foreclosure."

See also:

Aberdeen Bank v. *Chehalis County,* 166 U. S. 440, at page 461-462;
Collins v. *Johnston,* 237 U. S. 502, at page 507.

In *Chamberlain Machine Works* v. *United States,* 270 U. S. 347, Mr. Justice Sanford, speaking for this Court, says (p. 349):

> "The general allegations of 'fraud' and 'coercion' were mere conclusions of the pleader; and were not admitted by the demurrer. To show a cause of action it was necessary that the petition state distinctly the particular acts of fraud and coercion relied on, specifying by whom and in what manner they were perpetrated, with such definiteness and reasonable certainty that the court might see that, if proved, they would warrant the setting aside of the settlement. * * * The petition contained no such specific allegations; and since its vague and general averments did not overcome the effect of the release, the demurrer was properly sustained."

There are no allegations in this complaint (except the mere conclusions of law contained in them) which charge any unconscionable conduct on the part of the defendants or any violation of their duties as trustees. The ultimate facts upon which the majority opinion of this court is predicated is that the appraisal of the Duquesne Gas assets was excessive and fraudulent; that the circulars which

Furlaud & Company, Inc. issued in connection with the sale and disposition of the bonds and notes of Duquesne Gas Corporation grossly and fraudulently misrepresented the value of the property by which they were secured.

These facts, however, were never alleged in the complaint nor were there any allegations in the complaint from which it could be inferred that plaintiff intended to rely upon them.

Moreover, even if we had made no objection to the introduction of this testimony and even if no stipulation had been entered into by which it was agreed that we were to have a general exception to this entire line of testimony and even if the Court had not at the end of plaintiff's case confirmed this stipulation by stating to the effect that we may have an exception to this line of testimony, and even if we had not at the end of the case made a motion to dismiss the complaint, we feel that under the tradition of this Court as established by its decisions, in the absence of an amendment to conform the pleadings to the proof, plaintiff could not recover upon those facts.

As stated by Mr. Chief Justice Marshall in *Crockett* v. *Lee*, 7 Wheat. 522:

> "The hardships of a particular case would not justify this tribunal in prostrating the fundamental rules of a court of Chancery—rules which have been established for ages, on the soundest and clearest principles of general utility. If the pleadings in the case were to give no notice to the parties or to the Court of the material facts on which the right asserted was to depend, no notice of the points to which the testimony was to be directed, and to which it was to be limited; if a new case might be made out in proof, different from that stated in the pleadings, all will perceive the confusion and uncertainty

which would attend legal proceedings and the injustice which must frequently take place. The rule that the decree must conform to the allegations, as well as to the proofs of the parties, is not only one which justice requires, but one which necessity imposes on Courts.

In the case of *Garrett* v. *Louisville & N. R. Co.* 235 U. S. 308, at page 312, this Court says:

> "Every bill must contain in itself sufficient matters of fact, *per se,* to maintain the plaintiff's case; and if the proofs go to matters not set up therein the court cannot judicially act upon them as a ground for decision, for the pleadings do not put them in contestation.

As far back as in the case of *Foster* v. *Goddard,* 1 Black 506, this Court per Mr. Justice Swayne said (p. 518):

> "In equity proceedings the proofs and allegations must agree. A party can no more succeed upon a case proved but not alleged, than upon a case alleged, but not proved."

If this line of testimony were inadmissible under the complaint herein, as we think we have demonstrated that it was, how could the plaintiff have amended his complaint at the end of the trial or during the trial so as to render it admissible without at least giving to the defendants full opportunity to answer and to procure evidence to meet it?

If we are right in the foregoing, it indubitably follows that the evidence tending to establish the fact that the property conveyed to Duquesne Gas Corporation was greatly overvalued and that material misrepresentations as to the value of the property were made to the purchasers of securities, under the complaint as filed, should be disre-

garded. That these facts are not alleged in the complaint is too obvious to require argument, and was conceded by counsel for the complainant upon the oral argument before this Court. That the establishment of these supposed facts is essential to plaintiff's right of recovery is demonstrated by the majority opinion of this Court. We have always contended and still do that without the establishment of these facts no cause of action is alleged in the complaint and we believe that both the majority and minority opinions of this Court sustain us in this view.

This Court stresses the fact that the defendants offered no evidence to establish the value of the property conveyed at the time of its conveyance.

We respectfully ask how could the defendants have properly met that issue at that time? The case was on trial and defendants had no notice that that issue existed in the case.

However, it is in evidence that between the acquisition of the options in this case and the closing of the deal, a very large well, producing 7,000,000 cubic feet of gas per day, was brought in on the Nuss property (R. 64). Nuss testified that he was producing 700,000,000 cubic feet of gas a year (R. 60). This well alone would, if it continued to produce at that rate, have furnished the corporation with three times the amount of gas that all of the other wells owned by Nuss had in the past produced. It, doubtlessly, in the opinion of the experts, gave an enhanced value to a large additional acreage. Defendants did not have the expert who made the appraisal available. The preparation of an issue of this kind requires time and research and defendants were not given the opportunity to prepare their case upon this subject. They were never advised that the issue existed.

Again, the report of Barrow, Wade, Guthrie & Co. showed that the very combination of these properties had the effect of enhancing their value to a single corporation operating all of them (R. 194). Before they were combined, they had nine sets of executives, nine selling organizations, and eight independent drilling outfits. After they were combined they had one executive staff, one selling agency, one engineering staff.

We do not contend that this one organization did not cost more than any one of the nine organizations composing the group, but we do insist that the saving was tremendous. To prepare the evidence upon this subject would have required more time than was available to defendants after the case was actually on trial.

There is no question made but that the Duquesne Gas Corporation had ample natural gas to fully supply the requirements of that district of Pennsylvania which it served and that if this market had continued even as it existed in 1929 and 1930, the enterprise would have been completely successful.

This market, as a result of the industrial depression, was so curtailed that the amount of gas sold was hardly sufficient to cover the overhead and depletion charges. But, except in the most general way, this testimony was not available to the defendants. It would have required much time and intensive research to have procured admissible testimony upon this subject. It would have required at least the investigation of the requirement before and after 1930 of the principal customers who were large industrial manufacturers to show not only what the facts were but what were the reasons for the falling off of this market. We are advised that one customer alone, whose normal annual requirements prior to 1931 amounted to approximately two

hundred thousand dollars, used less than fifty thousand dollars of fuel gas in 1931.

What we are here trying to demonstrate is that it would have been impossible at the trial of this case to have properly prepared to meet this issue.

II.

We believe that this Court, in distinguishing this case from the principles of law announced by Mr. Justice Holmes in *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206, has overlooked certain substantial equities, the consideration of which we now urge upon it.

First, in this case, as in the *Lewisohn* case, the promoters organized their own company, transferred property to it and received in exchange the securities of their own corporation. That the defendants in the case at bar had first felt out the market and determined that they could market the securities so received is true.

That Lewisohn and Bigelow created a market for the stock of the Old Dominion Copper Mining & Smelting Company, and, after disposing of the stock of the corporation, bailed themselves out and made great profits, is also true.

Had these defendants retained these securities, we do not think that any one could have said that any wrong was done to any one. As stated in the *Lewisohn* case:

> "At the time of the sale to the plaintiff, then, there was no wrong done to any one. Bigelow, Lewisohn, and their syndicate were on both sides of the bargain, and they might issue to themselves as much stock in their corporation as they liked in

> exchange for their conveyance of their land" (p. 212).

So, in this case, if there had been no sale of securities to the public there could have been no wrong done to any one. The parties could have issued to themselves as many securities as they liked in exchange for the conveyance of their land. Certainly, there could have been no wrong done to the corporation. The promoters and the corporation were one.

Again, quoting from Mr. Justice Holmes' opinion:

> "If there was a wrong, it was when the innocent public subscribed. But what one would expect to find, if a wrong happened then, would not be that the sale became a breach of duty to the corporation nunc pro tunc, but that the invitation to the public without disclosure, when acted upon, became a fraud upon the subscribers from an equitable point of view, accompanied by what they might treat as damage. *For it is only by virtue of the innocent subscribers' position and the promoters' invitation that the corporation has any pretense for a standing in court.* (Italics ours).

We believe that that is true in this case.

This Court, in the *Lewisohn* case, very definitely suggested that any purchaser of securities would have a personal cause of action against the promoters in the event that any fraud was practiced upon him, but that the corporation would not as the result of such facts have a cause of action.

In considering the equities, it must be remembered that in cases such as this, when a receiver of a corporation is appointed, the market price of its bonds and notes fall to a very small fraction of their original cost to the public and

are picked up by speculators at such prices. Duquesne bonds and notes were at the time of the institution of this suit selling at five, six and seven per cent. of their par value.

So that by the time a suit of this kind comes to this Court for decision the parties who are or were interested in such securities naturally fall into three classes—first, those original subscribers of securities who held them from the beginning, second those purchasers of securities who bought them at high prices but who were compelled to or did part with them at a fraction of that cost, and third, speculators, who after the appointment of the receiver, purchased these securities at a small fraction of their cost.

As to the first class, they have their cause of action against the promoters from whom they can secure complete indemnity for the wrong done them; but under this decision they secure indemnity a second time and thereby subject these promoters to a double liability for the same act. As to the second class, they of course have their cause of action against the promoters and are entitled to secure full indemnity, but by reason of the fact that they have disposed of their securities they receive no additional benefits under this decision.

As to the third class, they have no cause of action against the promoters. They are mere speculators and with full knowledge of the situation purchased bonds and notes at extremely low prices. Yet, under this decision, they are unjustly enriched, and, as a result thereof, the promoters are again subject to a double liability; that is to say, the promoters must pay to the members of the second class full indemnity for the wrong which they suffered and the promoters have to pay the third class the same indemnity for wrongs not suffered by them.

Referring for a moment to the stockholders, if they were induced to make any purchases by reason of any false statement made by Furlaud & Company, they have their cause of action and are entitled to secure full indemnity in their individual capacities. But in reorganizations the holders of such equities are practically eliminated.

Here again this decision subjects the promoters to a double liability.

Assuming then that the promoters are able merely to pay the claims of those who may have causes of action against them in their own right, the effect of this decision would seem to us to deprive the second class of purchasers and the stockholders of substantial rights by rendering their debtors financially unable to pay them in full, and to unjustly benefit the first class, and the speculators who had purchased their securities for a song.

We believe that this Court may upon further consideration come to the conclusion that any party who was injured by any false valuation of the property conveyed to Duquesne Gas Corporation should be permitted to vindicate his own rights in a direct proceeding brought by him for that purpose rather than through the instrumentality of this action which gives to one class of litigants the right to recover twice the amount of indemnity to which it is entitled, to another class a profit to which it is not entitled and to a third class no indemnity whatever except such as it can secure by independent proceedings. This decision has the effect of making his recovery in independent actions much less valuable than if this decision had not been rendered, and, in addition, imposes on these promoters double liability for the same wrongs.

We do not believe that this court will seriously doubt that the parties who were injured or thought that they

were injured by the acts of these promoters or by other promoters similarly situated have vindicated or can and will vindicate their own rights.

Moreover, this decision does not and cannot protect the promoters from suits of this character. It merely has the effect of subjecting the promoters to the necessity of twice paying for the damages which they may have caused if they are able to do so.

Nor do we think that viewing the situation from its equitable and practical aspects this Court will assume that promoters of this character will be able to respond to the double liability imposed upon them by this decision. What we are trying to make clear is that the rule embodied in this decision must have the effect of unjustly enriching speculators who have purchased their bonds or notes with full knowledge of all the facts and, to that extent, destroy the rights of purchasers of bonds, notes and stock who may have just causes of action against promoters, who by this rule are rendered unable to meet such just claims.

Moreover, we feel impelled to call the attention of this Court to the following additional facts concerning the stock of Duquesne Gas Corporation.

This stock was all stock without par or nominal value. The original block of 1,000 shares of this stock was purchased by Furlaud & Company, Inc. for 50 cents per share. At that time they were the sole stockholders of the corporation.

A second block of 139,000 shares was sold to Furlaud & Company at 50 cents a share. It still was the sole stockholder of the corporation. Assuming that the remaining stock issued—535,000 shares having no par value—was issued without consideration of any kind to Furlaud & Com-

pany or its agent, how could that transaction have injured Duquesne Gas Corporation? Prior to the issuance of this stock Furlaud & Company owned all of the equity represented by stock in that corporation—Duquesne Gas Corporation had no other stockholder. After that transaction Furlaud & Company still owned all of the equity represented by stock in that corporation. The position of the corporation was not in the slightest degree altered. Before that occurred, all of the stock of the corporation belonged to identically the same interests as it did after the stock was issued. If this transaction had not taken place and Furlaud & Company had caused the stock of the corporation owned by it to be split up into 675,000 shares of stock without nominal or par value, how could that transaction have injured Duquesne Gas Corporation? Whatever equity there was in that corporation was represented by stock and belonged to Furlaud & Company, just as fully before the issuance of the stock to Kingston Corporation as it did afterwards. Nothing resulted from this transaction that could have affected Duquesne Gas Corporation either injuriously or beneficially. The stock ownership was merely evidenced by a greater number of pieces of paper which altogether amounted to no more and no less than that which existed before.

In the resale of this stock, injury may have resulted to someone but certainly no injury could have resulted to Duquesne Gas Corporation. The issuance of this stock could not and did not affect its solvency or insolvency. If the purchasers of this stock acquired a cause of action as the result of their purchases, Duquesne Gas Corporation was not in any degree affected thereby.

There is no evidence in this case that any false representations were made to any purchasers of this stock. The

learned Trial Court found as a fact that there was no such evidence (R. 231-232).

If we assume (as is a fact) that a reorganization of Duquesne Gas Corporation took place it is hardly necessary to point out how little the rights of these stockholders would have been considered in such a reorganization.

The value of their causes of action, so clearly recognized in the *Lewisohn* decision, is in effect in part at least taken away from them by this decision, if the effect of this decision should render the promoters insolvent and unable to meet the total obligations asserted against them. The point, however, which we are here urging is that the issuance of additional blocks of stock of no par value by this corporation to its sole stockholder did not and could not have resulted in any injury to it.

III.

Byron Corporation and Chaucer Corporation call this Court's attention to the fact that only 25 per cent. of the stock of each of these corporations belonged to the wives of Mr. Furlaud and Mr. Reuter respectively and that 75 per cent. of the stock of each of these corporations belonged to two other corporations concerning which no testimony was introduced by the plaintiff.

There is no evidence of any kind in this case that any of the stockholders of these corporations were chargeable with any improper conduct or with knowledge of improper conduct, unless a presumption at law exists that the wives of Furlaud and Reuter respectively are charged with knowledge of their husbands' acts. So far as Chaucer Corporation is concerned there is no direct evidence that

it made any sale or received any money as a result of this transaction. The only testimony on this subject is that of Mr. Roger A. McShea, Jr.

He testified (R. 99-100):

> "I did not examine the books of Chaucer Corporation." (R. 95).

Again at page 98 of the Record, he testified:

> "Of course, I did not see any books of any kind or any records as far as Chaucer were concerned."

At page 99 of the Record, the following testimony appears:

> "Q. Mr. McShea, either from conversations with Mr. Parisette or other members of his staff——
>
> Mr. Hirshfield: Whose staff?
>
> Q. (Continued) ——Furlaud & Company, Inc. or Maxime H. Furlaud or Carlos Reuter, talks with Mr. Parisette or other members of that office, examining the Bergen contract, examination of the Furlaud books, Byron books, Kingston books, were you able to construct an account of the sale of any other shares to Bergen & Company other than the 425,000 shares that you have testified about?
>
> A. No, sir.
>
> Q. I am not asking from books alone, I am asking from statements made by Mr. Parisette or otherwise?
>
> A. Those 425,000 shares to Bergen, is all I know of except what was apparently sold by Chaucer.
>
> Q. I am asking you about Chaucer. I am asking you if you have got any information in these examinations relating (fol. 143) to the matter of the sale by Chaucer?

A. Of course, I have the contract, but I believe from that, that Chaucer sold the same number of shares to Bergen that Byron did.

Q. Were any statements made to you by Parisette or others to that effect?

A. No, I don't believe so.

Q. Will you refresh your recollection by reading what I show you here?

A. I just don't know what you mean, Mr. Royall.

Q. Have you read this, '85,000 shares sold to Bergen', where did you get that from?

A. From my assumption, in accordance with the contract, that Chaucer also sold 42,500 shares, I worked this up on that assumption, which was based upon the contract.

Q. You assumed that the contract was performed 50-50, as the contract on its face indicated it was intended to be?

A. Yes, sir.

Q. And that upon that assumption, if it was performed 50-50, as the contract on its face indicated it was intended to be?

A. Yes, sir.

Q. And that upon that assumption, if it was performed 50-50, Chaucer sold another 42,500 shares to Bergen?

A. That is right.

Mr. Hirshfield: I object to that ground of assumption.

Q. I mean that is the best you can testify on that score?

A. Yes."

Recurring to the question of whether or not the wives of Furlaud and Reuter are as a matter of law chargeable with knowledge of the acts of their husbands, not only are

they not so chargeable but on the contrary, the law presumes them to be innocent of any such knowledge and the presumption to that effect must be overcome by affirmative evidence.

In *Gottlieb* v. *Thatcher,* 151 U. S. 271, this Court says (p. 279):

> "The relationship of the parties does not, of and in itself, cast suspicion upon the transaction, or create such a prima facie presumption against its validity as would require the Court to hold it to be invalid without proof that there was fraud on the part of the grantor, participated in by the grantee. This proposition is so well settled that authorities need not be cited in its support."

In the case of *Shultz* v. *Hoagland,* 85 N. Y. 464, the Court of Appeals says:

> "The relationship of assignor and assignee, and their intimacy and friendship, and the preference given to the latter as a creditor prove nothing by themselves. They are consistent with honesty and innocence, and become only important when other circumstances, indicative of fraud, invest them with a new character and purpose, and transform them from equivocal and ambiguous facts into positive badges of fraud" (p. 468).

But there were no other circumstances in this case which imputed guilty knowledge to either Mrs. Furlaud or Mrs. Reuter or to any other stockholders of these corporations.

Moreover, as a matter of common experience it seems extremely unlikely that a husband would confide in his wife anything that would reflect upon his conduct. It is true that the complaint makes certain very definite charges

to the effect that these corporations were mere instrumentalities of Furlaud and Reuter but no evidence was offered tending to establish that fact. We respectfully submit that there is no evidence in this case of that character. At most it is shown that these corporations acquired from Kingston Corporation an option to purchase from that corporation 510,000 shares of Duquesne Gas Corporation Common Stock at 50 cents per share. This was as much as had ever been paid for that stock. They exercised their option and paid for the stock. If Chaucer participated in the sale to John J. Bergen of which there is no evidence, the most that could be said was that it resold at a profit part of the stock purchased. The assumption that any person connected with either of these corporations had knowledge of any fact that would render the transaction improper is based upon pure speculation and is not supported by testimony in this case.

As to Chaucer Corporation there is no direct evidence that it ever received one cent from John J. Bergen. Mr. Bergen is a well known operator. It would have been very easy for the plaintiff to have put him on the witness stand to establish any facts that he desired to establish with reference to the source from which he obtained his stock. But it must also be remembered that Furlaud & Company had 140,000 shares of this stock. As far as Chaucer Corporation is concerned there is no more proof that it actually consummated this deal with Mr. Bergen than that he acquired that stock from Furlaud & Company. There is no direct evidence that he acquired it at all. The only witness who testified on this subject stated that he had not examined the books or records of any kind so far as Chaucer Corporation was concerned, that no one had told him that Chaucer Cor-

poration had received these sums of money and that he merely assumed that it had.

As to both of the corporations, however, we respectfully insist that no evidence of guilty knowledge on their part is disclosed by the evidence.

They were not parties to any transaction with Duquesne Gas Corporation.

If there were any fraud perpetrated upon the ultimate purchasers of this stock it was a fraud participated in by the Duquesne Gas Corporation providing the same representations were made to such purchasers as this Court has found were made to purchasers of bonds and notes. The effect of this decision would seem to give the Receiver of Duquesne Gas Corporation the right to recover sums that could never have been justly due it, at the expense of those to whom those sums were justly due.

If there were any impropriety in the appraisal of the properties transferred to Duquesne Gas Corporation there is no evidence in this case that any stockholders of these corporations had any knowledge of such fact. They acquired their stock in Duquesne Gas Corporation long after it had been issued to Kingston. They paid for it an amount greatly in excess of its value to Duquesne Gas Corporation or to any one else. If they or either of them sold part of the stock so acquired at a profit, it is not contended that in making this sale they made any representations of any kind to any one. Such transaction, if participated in by Chaucer Corporation, was with the broker to whom it is not shown that any representations were made by any one.

As to the right of this corporation or its receiver to recover on behalf of the creditors for stock issued by it for inadequate consideration or no consideration, this Court in the case of *Fogg* v. *Blair, supra,* states:

"It is averred in the bill, and the demurrer admitted, for the purposes of the hearing below, that full and adequate compensation for the work done by Blair and Taylor was $12,000 per mile in the company's first mortgage bonds. Assuming this to be true, if the stock issued to Blair and Taylor was of any considerable value at the time they received it, or if the circumstances attending its delivery to them indicated bad faith upon their part or upon the part of the corporation, different questions would arise from those now presented. But the bill contains no allegation whatever as to the real or market value of the stock. The court cannot say from any facts set forth in the bill as to the condition of the railroads in question, that the stock when delivered to the contractors was worth par, or that it had any substantial value. If, when disposed of by the railroad company, it was without value, no wrong was done to creditors by the contract made with Blair and Taylor. If the plaintiff expected to recover in this suit upon the ground that the stock was of substantial value, it was incumbent upon him to distinctly allege facts that would enable the court—assuming such facts to be true—to say that the contract between the railroad company and the contractors was one which, in the interest of creditors, ought to be closely scrutinized. He seems to have carefully avoided making any allegation as to the real or probable value of the stock, and to have supposed that the court, in the absence of averment or proof to the contrary, would assume that it was worth par or had substantial value."

The entire theory of the complainant in this case and the conclusion that must necessarily follow from the majority decision of this Court is that these additional pieces of paper representing stock in Duquesne Gas Corporation delivered

to Kingston had no value of any kind. If the facts upon which the majority opinion of this Court was based could not have been overcome by evidence, it must follow that the stock issued by Duquesne Gas Corporation was utterly and completely worthless and that no harm to any one could result from the issuance of the additional stock referred to.

There was no evidence in this case that any false representations were made to any purchaser of this stock. Certainly these corporations made none—nor are they charged with knowledge of any fact that would impute knowledge to them. The learned Trial Court found as a fact that there was no such evidence (R. 231-232). We, therefore, must respectfully urge that the issuance of this stock by Duquesne Gas Corporation could have resulted in no injury to it, first because the parties to whom it was issued owned all of the stock equity in the corporation before it was issued and owned no more after they received it, second, because in the re-sale of this stock no misrepresentations were either alleged or proven, and third because under the theory of the decision herein the stock issued had no value.

For the foregoing reasons it is respectfully urged that this petition for a rehearing be granted, and that the judgment of the United States Circuit Court of Appeals for the Second Circuit be, upon further consideration, affirmed.

Respectfully submitted,

LOUIS B. EPPSTEIN,
Counsel for Petitioners.

Certificate of Counsel.

I, Louis B. Eppstein, counsel for Maxime H. Furlaud, Kingston Corporation, Byron Corporation and Chaucer Corporation, the above-named defendants, petitioners herein, certify that the foregoing petition for a rehearing of this cause is presented in good faith and not for delay.

LOUIS B. EPPSTEIN,
Counsel for Petitioners.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935

No. 26

GEORGE W. McCANDLESS, as Receiver of DUQUESNE GAS CORPORATION,

Complainant,

against

MAXIME FURLAUD, KINGSTON CORPORATION, BYRON CORPORATION and CHAUCER CORPORATION,

Defendants.

PETITION FOR REHEARING ON BEHALF OF CHAUCER CORPORATION, ONE OF THE DEFENDANTS BELOW

JOAB H. BANTON,
Solicitor for Defendant, Chaucer Corporation.

SAMUEL I. HARTMAN,
CHARLES BALLON,
Of Counsel.

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Defendants.

PETITION FOR REHEARING ON BEHALF OF CHAUCER CORPORATION, ONE OF THE DEFENDANTS BELOW

To The Honorable Charles E. Hughes, the Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

The above-named defendant, Chaucer Corporation, by its solicitor, Joab H. Banton, presents this, its petition for a rehearing of the above-entitled cause insofar as the same involves and pertains to the Chaucer Corporation and insofar as a judgment has been awarded against said Chaucer Corporation in the sum of $425,000, with interest from June 6th, 1930.

Jurisdiction

The petition for certiorari in this cause was filed on April 18th, 1935, and certiorari was granted on May 13th, 1935. This Court rendered its decision on November 11th, 1935, reversing the judgment of the United States Circuit Court of Appeals for the Second Circuit and modifying its judgment in other respects including the award of judgment in the sum of $425,000, with interest from June 6th, 1930, against the defendant Chaucer Corporation as against whom the complaint was dismissed in the District Court, which was affirmed in the Court of Appeals.

Reasons for Petition for Rehearing

I.

There is not a scintilla of evidence in the record that Chaucer Corporation sold any stock of the Duquesne Gas Corporation nor that Chaucer Corporation received any money from any such transaction. The sole testimony at all relevant to this subject was that adduced through an accountant, one Roger A. McShea, Jr., plaintiff's witness. He testified in part as follows:

> "I also examined the books of the Byron and Kingston Corporation, as well as Furland & Company, *but I did not examine the books of Chaucer Corporation.*" (Italics ours.) (R. p. 95.)

Again at page 98 of the Record, Mr. McShea, desirous of clearly stating that he had no knowledge concerning Chaucer Corporation, testified:

"Of course, I did not see any books of any kind or any records as far as Chaucer were concerned." (Italics ours.)

Thereafter Witness McShea testified that he *assumed* that Chaucer Corporation sold 42,500 shares of Duquesne Gas Corporation. His exact testimony on *direct* examination follows:

"Q. I am asking you about Chaucer. I am asking you if you have got any information in these examinations relating to the matter of the sale by Chaucer? A. Of course, I have the contract, but I *believe* from that, that Chaucer sold the same number of shares in Bergen that Byron did.

Q. Were any statements made to you by Parisette or others to that effect? A. No, I don't believe so.

Q. Will you refresh your recollection by reading what I show you here? A. I just don't know what you mean, Mr. Royall.

Q. Have you read this, '85,000 shares sold to Bergen,' where did you get that from? A. *From my assumption*, in accordance with the contract, that Chaucer also sold 42,500 shares, *I worked this up on that assumption*, which was based upon the contract.

Q. You *assumed* that the contract was performed 50-50, as the contract on its face indicated it was intended to be? A. Yes, sir.

Q. And that upon that *assumption*, if it was performed 50-50, Chaucer sold another 42,500 shares to Bergen? A. That is right.

Mr. Hirshfield: I object to that ground of assumption.

Q. I mean that is the best you can testify to on that score? A. Yes." (Italics ours.) (R. pp. 99 and 100.)

The contract upon which the witness predicated his assumption is Plaintiff's Exhibit 31 and consists of a grant of an option to purchase Duquesne Gas Corporation common stock by Byron Corporation and Chaucer Corporation to one John J. Bergen. *This document is an option agreement, not a contract of purchase and sale.* No testimony was offered to show that Chaucer Corporation sold any Duquesne stock to Mr. Bergen or any one else. The lack of evidentiary strength and character in Witness McShea's testimony prompted counsel for plaintiff to ask him at the conclusion of this line of interrogation:

> "Q. I mean that is the best you can testify to on that score? A. Yes."

Mr. Justice Cardozo in referring to the Duquesne Gas Corporation stock in his opinion says:

> "Of the part belonging to Kingston, 85,000 shares were assigned to the Byron and Chaucer companies which sold them to the public through Bergen, a stock operator, for $850,000, $425,000 being paid to Byron and a like amount to Chaucer. What became of the other shares the record does not show." (80 Law. Ed. 74, at p. 78.)

It is respectfully submitted that the foregoing is an unwarranted assumption unsupported by the testimony in the case. Mr. John J. Bergen, referred to in the opinion, is a well known operator. It would have been easy for plaintiff to have put him on the stand and ascertain from whom he purchased his Duquesne stock holdings. It must be remembered that Furland & Company had 140,000 shares of Duquesne stock. So far as the record indicates there is

no more proof that Mr. Bergen consummated his purchase from Chaucer Corporation than from Furlaud & Company, Inc. The fact is that there is no direct evidence even that Mr. Bergen acquired any Duquesne stock at all. That the record is barren of evidence of a sale of Duquesne stock by Chaucer Corporation does not permit of contradiction.

II.

The Court's attention is respectfully directed to the fact that only 25% of the stock of Chaucer Corporation belonged to the wife of Carlos Reuter. The remaining 75% of Chaucer stock was owned by corporations as to which there isn't a single sentence of testimony in the record. The majority opinion of the Court however states that, "* * * Chaucer Corporation was closely related to Furlaud & Kingston, * * * the wife of Carlos Reuter (being) an important shareholder in Chaucer." (80 Law. Ed. 74, at p. 76.)

There is no evidence of any kind in this case that any of the stockholders of Chaucer Corporation were chargeable with any improper conduct or with knowledge of improper conduct unless the activity of Carlos Reuter is assumed to be improper and a presumption at law exists that his wife is charged with knowledge of her husband's acts. Carlos Reuter was not a stockholder of Chaucer Corporation; the record indicates only that Mrs. Reuter was a 25% stockholder. But such presumption does not exist,—on the contrary, the law presumes a wife to be innocent of any knowledge of her husband's improper conduct and the presumption to that effect must be overcome by affirmative evidence.

In *Gottlieb* v. *Thatcher*, 151 U. S. 271, this Court says:

> "The relationship of the parties does not, of and in itself, cast suspicion upon the transaction, or create such a prima facie presumption against its validity as would require the court to hold it to the invalid without proof that there was fraud on the part of the grantor, participated in by the grantee. This purpose is so well settled that authorities need not be cited in its support." (at p. 279.)

In the case of *Shultz* v. *Hoagland*, 85 N. Y. 464, the New York Court of Appeals says;

> "The relationship of assignor and assignee, and their intimacy and friendship, and the preference given to the latter as a creditor prove nothing by themselves. They are consistent with honesty and innocence and become only important when other circumstances indicative of fraud, invest them with a new character and purpose, and transform them from equivocal and ambiguous facts into positive facts badges of fraud." (at p. 468.)

Mrs. Reuter and other stockholders of Chaucer Corporation cannot be said then, to have had any knowledge of the alleged fraud. The Trial Court found as a fact that there was no such evidence. Such guilty knowledge can nowhere be found in the record and cannot be imputed to them at law.

This Court however has held herein that,

> "In view of the initial fraud the burden was on Kingston and Furlaud to show that Byron and Chaucer were purchasers in due course, and not agents and confederates wearing the cloak of purchasers. King v. Doane, 139 U. S. 166, 173, 35 L. ed.

84, 87, 11 S. Ct. 465; Canajoharie Nat. Bank v. Diefendorf, 123 N. Y. 191, 204, 205, 25 N. E. 402, 10 L. R. A. 676; Seymour v. McKinstry, 106 N. Y. 230, 240, 12 N. E. 348, 14 N. E. 94. We think that Byron and Chaucer were subject to an equal burden. Many suspicious circumstances point to guilty knowledge and justify a holding that the burden has not been borne." (80 Law. Ed. 74, at p. 84.)

In short, then, the theory upon which liability is imposed upon the Chaucer Corporation is that enunciated in the foregoing cases cited by Mr. Justice Cardozo in the majority opinion of the Court. Mr. Justice Harlan who wrote the opinion in the *Doane* case (*supra*), stated in part:

> "If the subscription and original note were obtained by fraud, these principles would determine this case adversely to Doane *unless he gave value for the original note without notice of the alleged fraud. Whether he did or did not give value, without such notice is the vital question in this case.* * * * *In the case supposed he must show that he paid value, that fact being established, he will be entitled to recover, unless it is proved that he purchased with actual notice of defect in the title, or in bad faith, implying guilty or wilful ignorance.* (Cases cited)." (at p. 173.) (Italics ours.)

The same rule is pronounced in the *Diefendorf* case (*supra*).

Applying this rule to the case at bar, it is respectfully urged that the complaint against Chaucer Corporation must be dismissed. It is apparent that value was paid by Chaucer Corporation for the Duquesne stock. This Court states in its majority opinion, "We are not unmindful of the con-

tention that the sale by Kingston (to Chaucer) was at the rate of 50 cents a share (which for 85,000 shares would amount to $42,500) * * *" (80 Law. Ed. 74, at p. 83). That this constituted full value cannot be questioned. The Court states in its opinion that "the Company (Duquesne Gas Corporation) became crippled and indeed insolvent at the outset of its business life." (80 Law. Ed. 74, at p. 80.) Certainly 50 cents per share of stock of an insolvent corporation is a good selling price. The record therefore shows no bad faith or knowledge of the alleged fraud in Chaucer Corporation and it further appears that said Chaucer paid full consideration for the shares of Duquesne stock purchased by it. Whatever burden may be imposed upon Chaucer Corporation, by virtue of the cases cited in this Court's opinion, has been amply sustained by it. Under the rule of the *Doane* case (*supra*), it is contended no judgment can be entered against the defendant Chaucer Corporation.

III

Assuming that Chaucer Corporation, in some esoteric manner not apparent in the record, has been shown to have been a party to or to have had knowledge of the alleged fraud, a cause of action against it does not lie in this complainant who is a receiver of the Duquesne Gas Corporation, the representative of the creditors of the corporation. In the *Doane* case (*supra*) the action was instituted by the *payee of a promissory note* against the maker. In the *Diefendorf* case (*supra*) the *plaintiff had purchased two promissory notes from the payee* thereof and instituted suit against the *maker*. In the third case cited by this Court in

its opinion, *Seymour* v. *McKinstry & Sabey*, 106 N. Y. 230, the action was instituted by a *vendor* of real estate to have an equitable lien declared in his favor for unpaid purchase money. In all cases the action was instituted by a party directly against the originator and creator of the instrument in question. The stockholders of Chaucer Corporation acquired their stock in Duquesne Gas Corporation long after it had been issued to Kingston. They paid for it an amount greatly in excess of its value to Duquesne or to any one else. There is no evidence that Chaucer sold any of the Duquesne stock, but even if it had and acquired a profit thereby, there is no contention that in effecting such supposed sale it made any representations of any kind to any one. Again, assuming that representations were made to induce the sale, then a cause of action might lie in such purchasers,—not in the receiver of the Duquesne Gas Corporation. The effect of this decision gives to the Receiver of Duquesne the right to recover sums that could never have been justly due it, at the expense of those to whom those sums were due. The District Court dismissed the complaint against the Chaucer Corporation and in connection therewith Mr. Justice Knox stated in his opinion:

> "However much the persons who subsequently purchased stock from Byron and Chaucer Corporations may have been injured, it does not seem that the receiver can recover on behalf of Dusquesne Gas Corporation under the doctrine announced in the case of the Old Dominion Copper Company v. Lwisohn, 210 U. S. 206. Nor can he recover, as in the case of the bonds and notes, on the theory that the money paid in by purchasers of stock became impressed with a trust in favor of the corporation. This is so for the reason that the evidence does not

show that any representation was made, by circulars or otherwise, that the money so received would be paid over to the Dusquesne Gas Corporation. The complaint therefore will be dismissed as against the defendants Byron Corporation and Chaucer Corporation."

For the reasons set forth hereinabove it is respectfully submitted that this petition for a rehearing be granted; that the judgment of the United States Circuit Court of Appeals for the Second Circuit be, upon further consideration, affirmed, and that the complaint herein be dismissed as against the defendant Chaucer Corporation.

Respectfully submitted,

JOAB H. BANTON,
Solicitor for Defendant,
Chaucer Corporation,
285 Madison Avenue,
New York City, New York.

SAMUEL I. HARTMAN,
CHARLES BALLON,
Of Counsel.

Certificate of Counsel

I, Joab H. Banton, solicitor for defendant, Chaucer Corporation, certify that the foregoing petition for a rehearing of this cause is presented in good faith and not for delay.

JOAB H. BANTON,
Solicitor for Defendant,
Chaucer Corporation.

SUPREME COURT OF THE UNITED STATES.

No. 26.—October Term, 1935.

George W. McCandless, as Receiver of Duquesne Gas Corporation, Petitioner, vs. Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation, Respondents.

On Writ of Certiorari to the Circuit Court of Appeals for the Second Circuit.

[November 11, 1935.]

Mr. Justice Cardozo delivered the opinion of the Court.

The suit is by a receiver of an insolvent corporation to compel its promoters and their confederates to restore illicit gains.

At the time of the challenged acts Maxime H. Furlaud was the president and principal shareholder of Furlaud & Company, Inc., a corporation now dissolved. For convenience the name Furlaud, unless qualified, will be used to designate the company. Carlos Reuter was an officer of the same corporation and a holder of a block of shares. He was named as a defendant, but was not served with process, and hence is out of the case, except in so far as his acts affect the liability of others. Kingston Corporation was a subsidiary of Furlaud and was owned and controlled by the same persons. Byron Corporation and Chaucer Corporation were closely related to Furlaud and Kingston, the wife of Maxime Furlaud being an important shareholder in Byron and the wife of Carlos Reuter an important shareholder in Chaucer.

Furlaud was known as an investment banking house, and was interested in the issue and sale of corporate securities. Particularly it was interested in a project for the formation of a company that would own and operate gas fields in Western Pennsylvania. Reuter, representing Furlaud, took options from the owners of nine separate tracts. These options, which at first were gratuitous, were acquired in the name of a subsidiary, Kingston. Engineers were then employed to examine the fields and appraise their value. One of them, Davis, made report to his employer in

February, 1930, that five of the tracts, which were afterwards acquired for about $1,300,000, had a value of about $1,700,000 at the time of the appraisal. The record permits the inference that the report was unsatisfactory to Reuter, who was hoping for a valuation that would make investment in the enterprise more attractive to the public. Accordingly the business of appraisal for the four remaining tracts was taken out of the hands of Davis and placed in charge of others. The new engineers were less conservative than their predecessor. They fixed the value of the four tracts at about $5,000,000, nearly five times the purchase price. Lands to be conveyed by Nuss for $660,000 figured in the appraisal as worth the price and a million over. A value of $850,000 was assigned to undeveloped acres which he agreed to convey for nothing. The purchase price for the nine tracts was $2,572,989; $7,000,000, or nearly that, was the appraisal for the whole. A witness for the complainant stated at the trial that the fair value of all the tracts was about $2,700,000, the cost and little more.

With the appraisals thus completed a company was organized in February, 1930, to take title to the gas fields covered by the options. This was the Duquesne Gas Corporation, now in the hands of the complainant as receiver. The options for the lands were still in the name of Kingston. Furlaud had made a payment ($45,510) to give them binding force, but title had not passed. The new company when organized had an authorized capital of 1,000 shares of no-par common stock. Furlaud subscribed for the whole issue, paying for the shares at the rate of 50 cents a share. The nominees and representatives of Furlaud were then the sole stockholders. They were also the sole directors. Provision was made afterwards for an increase of the capital stock, but of this there will be more later.

With the options still outstanding Furlaud formed a syndicate of bankers to market the securities. The syndicate published an advertisement in a newspaper inviting subscriptions by the public to an issue of bonds and notes. There were to be $4,000,000 6% mortgage bonds (to be sold at 97½%), and $1,000,000 6½% mortgage notes (to be sold at 98%). Each circular contains the caption "purpose of issue". In the bond circular the statement is: "These bonds are issued by the corporation in connection with the acquisition of properties, and to provide cash for develop-

ments, extensions and other corporate purposes." There is a like statement in the other circular as to the purpose of the notes. Investors were informed that the appraisals of the engineers covering the properties of the corporation, including working capital of $365,000, aggregate $7,038,000, the properties examined by Davis being appraised at $1,743,520, and those examined by his successors at $4,929,787. The circulars as first drafted lumped the two appraisals as if they had been the work of the two appraisers jointly. Davis objected, with the result that the appraisals became several.

In the meantime Duquesne was preparing the resolutions and agreements that would be necessary to satisfy the bankers. On March 5, 1930, the directors, still dominated by Furlaud, authorized the increase of the capital stock to 1,250,000 shares. On April 3, Furlaud subscribed for 139,000 shares at 50 cents a share. On April 7, Duquesne agreed with Kingston to take over the gas fields covered by the options as soon as Kingston got the title. The consideration was to be cash in the sum of $3,015,000 (which was $565,100 more than Kingston was expected to pay to the grantors); bonds of the par value of $1,300,000, part of the forthcoming issue; and 535,000 shares of no-par stock. On the same day there was an agreement between Duquesne and Furlaud whereby Furlaud agreed to take all the forthcoming mortgage notes ($1,000,000) at a price of 88%; and $2,700,000 mortgage bonds at a price of 90%. The whole issue of mortgage bonds was thus divided up between Furlaud and its subsidiary, Kingston, $2,700,000 to the one and $1,300,000 to the other. Furlaud and Kingston being one, the situation was the same in substance as if Furlaud had taken them all.

The public offering of the bonds was a spectacular success. It began on March 25. By the first week of April subscriptions of the par value of $2,350,000 were on hand, and other subscriptions were coming in from day to day. The responses made it clear that an avid and credulous public would absorb the entire issue. Furlaud could safely go ahead and exercise the options, for at the pace subscriptions were coming in the proceeds of the bonds would pay for all the gas lands and leave a handsome margin over. Even so, there was need of ingenuity to work out a plan that would synchronize the two transactions, the cashing of the subscriptions and

the payment for the lands. The cash would not be paid on the subscriptions till the bonds with the deed of trust were ready for delivery, and delivery was impossible until Duquesne, the mortgagor, had title to the fields. A way had to be found for providing the money necessary to get possession of the deeds, which had been placed by the grantors in escrow with banks in Western Pennsylvania. A way had to be found also for making the proceeds of the subscriptions available as a fund that could be applied with a minimum of delay upon account of the purchase price. To those ends Maxime Furlaud made arrangements with the Central Hanover Bank & Trust Company of New York that for one day the Kingston Corporation should have a credit with the trust company of $3,015,000, and the Furlaud Company for the same time a credit of $3,379,500. The day chosen for that purpose was April 9. The credits would be used to procure title to the lands and to supply the new corporation with a fund of working capital. The subscriptions would be used so far as possible to liquidate the credits. Precautions were taken to make certain that the credits would be applied to the expected uses and not otherwise. In the words of a witness, "the bank always had a string on the money."

The appointed day arrived. Kingston drew against the credit of $3,015,000 set up in its favor, and delivered certified checks to banks in New York with which to meet drafts drawn by those banks on the banks in Western Pennsylvania. The amount thus withdrawn was $2,449,900. On report by telephone and telegraph that the checks had been received the Pennsylvania banks released the deeds from escrow and caused them to be placed on record. Title being thereby vested in the mortgagor, the mortgage bonds were handed over to the trust company for transmission to the banking houses that had collected the subscriptions. A long queue of messengers, employed by these houses, was on hand throughout the day with checks from the subscribers for delivery against the bonds. Nearly $2,000,000 (if the defendants' figures are accepted, $1,886,330) was paid then and there upon account of the subscriptions with other payments close at hand. What was paid from these sources was turned over to Furlaud, who applied it at once toward the liquidation of the loan.

The loan had been fixed at the precise amount necessary to enable Furlaud to discharge its obligations to Duquesne. Of the

credit for account of Furlaud, $2,430,000 was used to pay for $2,700,000 bonds at 90; $880,000 for $1,000,000 notes at 88; and $69,500 for 139,000 shares of stock at 50 cents a share ($3,379,500 in all). But Duquesne was no sooner in receipt of the money than it paid the greater part out again. Of the $3,379,500, $3,015,000 was paid back to the Trust Company to be credited to the account of Kingston. This canceled the Kingston loan, reimbursed the Trust Company for the $2,449,900 withdrawn earlier in the day to obtain title to the lands, and left $565,100 over. This balance was not kept by Kingston. It was transferred at once to Furlaud; the circuit was then complete.

Furlaud had been well assured, when it closed the title on April 9, that there would be no difficulty in disposing of every bond and note. The event justified its faith. Within a few weeks all the remaining bonds had been converted into cash. Also within a few weeks the notes had been sold in bulk for $861,097.69 to a firm of investment bankers. Even the worthless shares of stock were unloaded on the public. The shares that were to go to Kingston (535,000) and those that were to go to Furlaud (139,000) were taken in the name of Parisette, one of Furlaud's employees. Of the part belonging to Kingston, 85,000 shares were assigned to the Byron and the Chaucer companies, which sold them to the public through Bergen, a stock operator, for $850,000, $425,000 being paid to Byron and a like amount to Chaucer. What became of the other shares the record does not show.

Checks and credits have now been traced through their bewildering entanglements. None the less when the process of analysis is over, it is legitimate to forget the details, and fix our minds on the results. The situation can be simplified without obscuring its essential features. Indeed only in that way will the realities of what was done be manifest.

After all the circuits had been traveled from one company to another and back to the point of origin, what had been accomplished for Duquesne and Furlaud stood out in clear relief. Duquesne had the ownership of gas fields, worth at cost about $2,500,000, though extravagantly appraised at many millions more. It had also $365,000 for working capital. True it had received $3,379,500, but it had paid out at once $3,015,000. The working capital was the difference ($364,500) together with $500 received for the

first issue of its shares. These are the credit items that any balance sheet must show. The liabilities were the bonds and notes and the no-par shares of stock. The bonds and notes, when distributed to the public, became liens for $5,000,000, more than $2,000,000 in excess of the cost of all the assets with working capital included. The shares of stock, issued in vast quantities, had nothing of substance back of them. If cost and value were about the same, there was thus insolvency at the beginning as well as at the end, unless the proceeds of the securities were devoted to the uses of the debtor, as the circulars published in the newspaper in effect stated they would be. Nothing of the kind was done. The bonds and the notes, instead of being used by Furlaud and its allies for the benefit of Duquesne, were disposed of as their own and at a large profit to themselves. The record supports the inference that some of the shares of stock were used in the same way. The promoters and their confederates pocketed the spoils. Less than two years later the victimized company was in the hands of a receiver.

The District Judge held that the appraisal of the Duquesne assets was excessive and fraudulent. "There is little doubt," he said, "that the circulars which Furlaud & Company, Inc., issued in connection with the sale and distribution of the bonds and notes of Duquesne Gas Corporation grossly and fraudulently misrepresented the value of the property by which they were secured." He held also that by force of the statements in the circulars as to "the purpose of the issue," the proceeds of the subscriptions were chargeable with a trust for the benefit of Duquesne and the holders of its mortgage debt. He gave judgment against Furlaud individually (the Furlaud Company was then dissolved) and also against Kingston for $1,554,779.73, with interest (a total of $1,834,640.08), which was the difference between the moneys realized by the promoters through the sale of bonds and notes ($4,492,768.73), and the amount paid to Duquesne and devoted to its proper uses ($2,937,989). He refused to give judgment against any of the defendants for the proceeds of the shares of stock. There were cross appeals to the Circuit Court of Appeals for the Second Circuit, Furlaud individually and Kingston appealing from the decree in so far as it held them accountable for the proceeds of the bonds and notes, and the receiver from so much of the decree as relieved all the defendants from liability growing out of the disposition of

the shares. Upon the first hearing of the cause, the Court of Appeals declined to pass upon the merits and dismissed the bill on the ground that the appointment of the ancillary receiver was void for want of jurisdiction. 68 F. (2d) 925. This court reversed, and remanded the cause for a determination of the merits. 293 U. S. 67. Upon a second hearing in the Court of Appeals the defendants were again the victors. The court took the view that Furlaud and Kingston had acted with the knowledge and consent of Duquesne, the promoters and their agents being then the only shareholders, and that under the doctrine of *Old Dominion Copper Co.* v. *Lewisohn*, 210 U. S. 206, the corporation, its incoming shareholders and the receiver were bound by that consent, whatever remedies might be available at the suit of a defrauded creditor. 75 F. (2d) 977. A second writ of certiorari brings the case to us again.

Promoters of a corporation stand in a fiduciary relation to it to this extent at least, that they will be chargeable as trustees if they deal with it unconscionably or oppressively or in violation of a statute, unless the liability for such misconduct has been effectually released. *Dickerman* v. *Northern Trust Co.*, 176 U. S. 181, 203, 204; *Brewster* v. *Hatch*, 122 N. Y. 349, 362; *Erlanger* v. *New Sombrero Phosphate Co.*, 3 App. Cas. 1218; affirming 5 Ch. Div. 73; *Gluckstein* v. *Barnes*, [1900] A. C. 240; *Yeiser* v. *United States Board and Paper Co.*, 107 Fed. 340, 344. To what extent the approval of all the shareholders will relieve them of that burden is a question not susceptible of answer without considering the nature of the wrong and the interests affected. To some extent their position is akin to that of directors, though the limits of their duty are less definite and certain. Even for erring directors, however, there may at times be absolution if all the shareholders are satisfied. *Holmes* v. *Willard*, 125 N. Y. 75. The interests affected by approval will shape the power to approve.

Old Dominion Copper Co. v. *Lewisohn* was a case where promoters made a sale to a corporation in return for shares of stock, the par value of the shares being greatly in excess of the cost to the sellers of the property conveyed. The existence of this profit was known to the shareholders, for the shares belonging to the promoters were all that had then been issued. There was no evidence that the effect of the transaction was to make the company insol-

vent or to work a fraud upon its creditors or to divert the assets to forbidden uses or to violate a statute. "At the time of the sale to the plaintiff . . . there was no wrong done to any one." 210 U. S. at p. 212. The grantors and their syndicate "were on both sides of the bargain, and they might issue to themselves as much stock in the corporation as they liked in exchange for their conveyance of their land." 210 U. S. at p. 212. Far from planning to defraud, "they believed in the enterprise" and "preferred to take stock at par rather than cash." 210 U. S. at p. 215. They had paid for the mines with their own money, and there were no creditors to be affected by anything they did. In such circumstances the ruling was that incoming shareholders, subscribing for new shares, were in the plight of those ahead of them and could have no better case. *Davis* v. *Las Ovas Co.*, 227 U. S. 80, declined to extend the ruling to a case where the approval was by less than all the shareholders and without disclosure of the facts to others.

Old Dominion Copper Co. v. *Lewisohn* does not rule the case at hand. The effect of the promoters' conduct here was to saddle the company with liens beyond the value of its assets, mortgaged and unmortgaged. Through the diversion of the proceeds of the subscriptions to the use of Furland and confederates, the company became crippled and indeed insolvent at the outset of its business life. True, the findings of the District Court do not state in so many words that the company in its beginnings was insolvent as well as crippled. They do state, however, that the appraisals were grossly and fraudulently and wantonly excessive. Cost in and of itself, though far from conclusive, is still evidence of value (*Parmenter* v. *Fitzpatrick*, 135 N. Y. 190, 199), especially where there is no market value in the strict or proper sense. *Sinclair Refining Co.* v. *Jenkins Petroleum Process Co.*, 289 U. S. 689, 697. In this case a witness for the complainant places a valuation upon the property in substantial correspondence with the cost. There is no opposing evidence in behalf of the defendants, and so the District Judge points out. In that state of the record, the promoters had the burden of answering and repelling the inculpatory evidence by proof that they had been true to their fiduciary duties and that their conduct had been fair and just. *Geddes* v. *Anaconda Copper Mining Co.*, 254 U. S. 590, 599; *Matter of Smith*, 95 N. Y. 516, 522; *Allen* v. *La Vaud*, 213 N. Y. 322, 326. The public

had been invited to invest in the securities on the representation that the proceeds would be used for the purchase of the lands and for cash capital necessary or useful for the business. In fact about three fifths of the money was applied to the designated uses, the rest being kept for the use of the promoters. If this could be done without cutting down the value of the assets below the mortgage debt, the act would be so near to magic as to call for explanation from promoters not professing to be magicians. No word of explanation was offered at the trial or is now suggested in the briefs. In those conditions, only one legitimate inference was open to the trier of the facts, and this he must be taken to have drawn. The appraisals having been shown to be fraudulent, the one legitimate inference to be drawn from the defendants' silence was that the value of the lands was not greater than the cost, at least in any large amount. If that be so, the company was made insolvent at the outset when the proceeds of the subscriptions were devoted to the use of the promoters.

No consent of shareholders could make such conduct lawful when challenged by the receiver as the representative of creditors. If the shareholders and the directors had combined with the promoters to despoil the corporation and defeat the remedies of creditors by a gift of half the assets, the gift could have been annulled either by the creditors directly or in their behalf by a receiver. *Casey* v. *Cavaroc*, 96 U. S. 467, 489, 490; *Atlantic Trust Co.* v. *Chapman*, 208 U. S. 360, 371; *Hamor* v. *Taylor-Rice Engineering Co.*, 84 Fed. 392, 399; *American Can Co.* v. *Erie Preserving Co.*, 171 Fed. 540, 542; *Sweet* v. *Lang*, 14 F. (2d) 758, 760; *Gillett* v. *Moody*, 3 N. Y. 479; *Pittsburgh Carbon Co.* v. *McMillin*, 119 N. Y. 46, 53. The distinction between such a situation and the present is one solely of degree. This is not a case where at the time of issuing the securities the shareholders and the promoters were the only ones concerned. Here at the moment of the conveyance the interests of bondholders and noteholders were put in jeopardy by a division of the proceeds that would make their mortgage worthless. The promoters could not receive for themselves or deliver to subscribers the bonds and notes of the company secured by deed of trust until title had been acquired to the lands covered by the deed. On the other hand, they could not pay the purchase price and acquire title to the lands without the proceeds of subscriptions, the contributions of the public. All this was known to

the shareholders and known to the directors, for the promoters were the shareholders and the directors men of straw. In its effect upon subscribers the transaction was the same as if the proceeds of the bonds and notes had been paid into the treasury of the company and then paid out to the directors for the use of their confederates. It was not within the power of the shareholders to legalize this waste to the detriment of others. It would not have been within their power to bring that result to pass though shareholders and promoters had been different persons, acting at arm's length. Still more clearly it was not within their power when shareholders and promoters were in substance the same persons. Cf. *California Calaveras Mining Co.* v. *Walls*, 170 Cal. 285, 299; *Pittsburgh Mining Co.* v. *Spooner*, 74 Wisc. 307. Consent in such conditions, so far as it gives approval to conduct in fraud of the rights of others, is a word and nothing more. It is not in concord with realities. There is no occasion to consider whether the corporation itself at the instance of new shareholders would be permitted to disaffirm the fraud and maintain a suit in equity for appropriate relief. We put that question by. Enough that the receiver has the requisite capacity. A court of equity has taken hold of the assets of this company, intangible assets as well as tangible, for administration as a trust in accordance with equitable principles. *Hollins* v. *Brierfield Coal & Iron Co.*, 150 U. S. 371, 380. Included in those assets are moneys fraudulently diverted to the prejudice of creditors. Cf. *McClure* v. *Law*, 161 N. Y. 78; *Bosworth* v. *Allen*, 168 N. Y. 157, 166. There is power at the instance of the receiver to bring them back into the trust.

These considerations without more would separate *Old Dominion Copper Co.* v. *Lewisohn* from the case before us now. Other aspects of the present case accentuate the division. What was done by the promoters here was in the teeth of a prohibition of the Constitution of Pennsylvania, the state where the corporation was formed and where its business was to be done. The Constitution of Pennsylvania provides (Art. 16, § 7): "... no corporation shall issue stocks or bonds except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." See also Act of April 17, 1876, P. L. 30, 32, § 4; Purdon's Penna. Stats., Title 15, § 131. The prohibition is not escaped through the receipt of some property or money if the amount or value is inadequate. *Big*

Springs Electric Co. v. *Kitzmiller*, 268 Pa. 34, 38; *Commonwealth* v. *Reading Traction Co.*, 204 Pa. 151; *In re Wyoming Valley Ice Co.*, 153 Fed. 787, 793; affirmed *sub nom. Wiegand* v. *Albert Lewis Lumber & Mfg. Co.*, 158 Fed. 608, 610. True, the securities are valid in the hands of innocent purchasers, whatever the consideration (*Guarantee T. & T. Co.* v. *Delworth Coal Co.*, 235 Pa. 594), but the liability of the directors or other fiduciaries who have put them into circulation is not thereby released. There are decisions in Pennsylvania that the Constitution is not self-executing. *Grange National Bank* v. *Collman*, 306 Pa. 200. That holding is irrelevant as to corporations such as this one, for there exists as to them an "implementing" statute (Purdon's Penna. Stats., *supra*), without restriction as to the form of remedy. Precedents exist for a suit at the instance of incoming shareholders, though the corporation was solvent and there was no injury to creditors. *Spangler Brewing Co.* v. *McHenry*, 242 Pa. 522, at p. 530. Precedents exist in cases of insolvency for a suit by a trustee as the representative of creditors, and this though they became such after the securities were issued. *Bingaman* v. *Commonwealth Trust Co.*, 15 F. (2d) 119 [D. C. M. D. Pennsylvania], and cases there collected; cf. *Coleman* v. *Teppel*, 230 Fed. 63, 70 [C. C. A. 3], affirming 229 Fed. 300; *In re Wyoming Valley Ice Co.*, *supra*; *Krebs* v. *Oberrender*, 274 Pa. 154; *Finletter* v. *Acetylene Light Co.*, 215 Pa. 86. No where is it held that delinquent fiduciaries who have nullified the statute may keep the profits for themselves when creditors will be injured unless the profits are returned. At times and for certain purposes the consent of shareholders may give validity to acts that would otherwise be voidable, if the only interests affected are those of the shareholders consenting. It can never be operative to the prejudice of others where consent is in derogation of the public policy of the state or the prohibition of a statute. *Central Transportation Co.* v. *Pullman's Car Co.*, 139 U. S. 24, 59, 60; *Kent* v. *Quicksilver Mining Co.*, 78 N. Y. 159, 185, 186, 187; *Sheldon H. B. Co.* v. *Eickemeyer H. B. M. Co.*, 90 N. Y. 607, 613; *Mann* v. *Edinburgh Northern Tramways Co.*, [House of Lords], 68 L. T. (N. S.) 96; *The Society of Practical Knowledge* v. *Abbott*, 2 Beav. 560, 568. This case is plainly within the scope of that exception. There was here a statutory prohibition, rooted in public policy. *Gearhart* v. *Standard Steel Co.*, 223 Pa. 385, 389. The shareholders were not at liberty, at all events to the prejudice of creditors or other share-

holders, present or prospective, to set that policy at naught. If the effect of what they did was to put illicit profits in the pockets of trustees, their consent will not avail to block pursuit and reclamation.

We have assumed in all this that the corporation was insolvent at the beginning of its business life. The assumption is well founded for reasons already stated, yet we do not need to go so far. Even though the company was not literally insolvent, the result would be the same. There would be a wrong to bondholders and noteholders if assets were depleted to the very brink of insolvency after fraudulent misrepresentations to the effect that there was an ample margin of security. What was taken out of the company in such circumstances would be taken subject to a trust and would so continue until the security thus depleted had paid the debt in full. The defendants do not assert that it is adequate for that today. Confusion of thought is inevitable unless the position of the wrongdoers as trustees is steadily kept in mind. What is here is something more than a tort of fraudulent representations to be redressed by the recovery of damages at the suit of the defrauded creditors. What is here is a tort growing out of the fraudulent depletion of the assets by men chargeable as trustees if they have failed to act with honor. There are important differences, moreover, between an overissue of stock, which may leave the assets unimpaired, and a withdrawal of cash, which puts the enterprise in peril. Cf. *Arnold* v. *Searing*, 78 N. J. Eq. 146, 162; 73 *id.* 262, 265, 266; *Eureka Mining Co.* v. *Lively*, 59 Wash. 550. The duty of reclaiming assets so diverted and holding the wrongdoers to their duty as trustees is one that rests on the receiver. It is not within the power of wrongdoers and shareholders by any compact between themselves to make the duty less.

In considering the effect of *Old Dominion Copper Co.* v. *Lewisohn*, we have spoken until now of the bonds and notes only. It is necessary at this point to say something about the stock. Of the total issue, 535,000 shares went to Kingston as a bonus. The only pretense of value was a conveyance of the gas fields covered by the options, which were worth, as we have seen, no more than Kingston paid for them. In return for the conveyance of these lands Kingston received $3,015,000 in cash or more than the actual value of anything conveyed. It also received bonds of the par value of $1,300,000; and last of all the stock. Plainly the stock was a bonus and nothing else.

Furlaud and Kingston, having made themselves parties to a scheme whereby Duquesne was to be despoiled and its creditors were to be defrauded, became accountable, we think, for everything that came to them as a result of the conspiracy in excess of the consideration furnished on their side. They were not trustees as to the bonds and notes, and lawful owners of the shares, but trustees as to all, the transaction being a unit, infected with a common vice. Everything of profit arising out of the abused relation must now be yielded up. Even after this is done, reparation will be incomplete. Restitution of the profits will not make up, without more, for the inadequacy of the overvalued land to return to the lienors their principal and interest. In such circumstances the shares like the bonds and notes must contribute what they can. The certificates, were they on hand, might be turned into the treasury of the company for sale, if they still had any value. The shares having been sold to others and the certificates being no longer subject to the mandate of the court, the trust that attached to them has been transferred to the proceeds, which when paid to the receiver will be used like other assets in reduction of the debts.

We are not unmindful of the contention that the sale by Kingston was at the rate of 50 cents a share (which for 85,000 shares would amount to $42,500), and that the sale for $850,000 was made by two other corporations, the Byron and the Chaucer. In view of the initial fraud the burden was on Kingston and Furlaud to show that Byron and Chaucer were purchasers in due course, and not agents and confederates wearing the cloak of purchasers. *King* v. *Doane*, 139 U. S. 166, 173; *Canajoharie National Bank* v. *Diefendorf*, 123 N. Y. 191, 204, 205; *Seymour* v. *McKinstry*, 106 N. Y. 230, 240. We think that Byron and Chaucer were subject to an equal burden. Many suspicious circumstances point to guilty knowledge and justify a holding that the burden has not been borne.

The respondents make the point that Maxime Furlaud is not subject to personal liability for wrongs committed by the Furlaud Company or Kingston. He was the head and front of the conspiracy. For anything done in fulfilment of the common purpose either by himself or by any of the corporations dominated by him, he and his confederates are liable *in solido*. *Mack* v. *Latta*, 178 N. Y. 525, 532; *Anderson* v. *Daley*, 38 App. Div. 505; 159 N. Y. 146; *Irving Trust Co.* v. *Deutsch*, 73 F. (2d) 121, 123; *Jackson* v. *Smith*, 254 U. S. 586, 589.

The objection is also made that testimony as to the value of the lands should have been excluded by the court as not within the pleadings. The complaint was based upon the theory that the promoters had been guilty of unconscionable conduct. Whether that was so could not be known without exploring the transaction to the depths and all the circumstances attending it. To this it may be added that the trial judge received the testimony provisionally and subject to a motion to strike when all the evidence was in. The motion was not made. Nor at any stage of the trial was there a motion to dismiss on the ground of a variance between the pleading and the proof.

Another objection is that the defendants should have been credited with expenses for commissions, attorneys' fees, printing disbursements and the like, expenses incidental, it is claimed, to the acquisition of the lands. A fund of $300,000 was set aside for that purpose. The record makes it clear, however, that only a part of this fund was necessary for expenses of any kind and that only a small part of the expenses, if any, were of such a nature as to be permissible deductions for parties to a fraud. It is likely that some items would be allowable, if properly identified. *Loos* v. *Wilkinson*, 113 N. Y. 485, 499; *Frank* v. *Von Bayer*, 236 N. Y. 473, 477, 478; *Randolph* v. *Scruggs*, 190 U. S. 533, 539. The difficulty is that we are unable on this record to determine their amount. The judge might have required the defendants to separate the good from the bad while the case was still on trial. Instead of doing this he put the defendants off their guard by saying that matters of that sort would be reserved for an accounting. Unless the receiver and the defendants find it possible to agree as to the allowance for expenses, an accounting will be necessary to determine what part of the $300,000, the total amount reserved, is an appropriate deduction.

Other objections put forward in argument at the bar can be dismissed in a few words.

If and when the defendants shall restore to the receiver the moneys taken unto themselves, it will be time enough to consider problems as to the marshalling of assets between creditors who were such at the commission of the wrong and those of later date. No attempt is made to forecast the answer now. The principles that govern the distribution of assets conveyed in fraud of creditors, present or prospective, and after such conveyance reclaimed by a

receiver, are adequate to work out justice, however great the complications.

We find it immaterial that the defendants or some of them may be liable to creditors in common law actions to recover damages for false representations as to the value of the assets. That is not the basis of the suit before us now. Moreover, the question is not here whether restitution of illicit profits as the outcome of this suit may be proved to mitigate the damages in actions by other plaintiffs, if any such there are. As we have striven to make clear, the receiver does not claim to have succeeded to the rights of bondholders or noteholders to recover damages for deceit. The wrong that is here redressed is the unlawful depletion of the assets whereby the company was made insolvent and the creditors were defrauded of their lawful rights and remedies.

The decree of the Circuit Court of Appeals reversing the decree of the District Court and dismissing the bill of complaint is reversed.

The decree of the District Court is modified by increasing the recovery against the defendants Maxime H. Furlaud and the Kingston Corporation in the sum of $850,000 with interest from June 6, 1930, when the shares of stock were sold, and by the award of judgment against the Byron Corporation in the sum of $425,000 with interest from June 6, 1930, and against the Chaucer Corporation for the same amount.

There will be a further modification by the allowance to the defendants Furlaud and the Kingston Corporation of so much of the sum of $300,000 as may be found on an accounting to have been disbursed for expenses that are chargeable in equity to the Duquesne Corporation, unless the amount of such allowance is fixed by agreement, approved by the court to which the receiver is accountable, in which event the judgment against those defendants shall be reduced accordingly.

The decree of the District Court as thus modified is affirmed.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 26.—October Term, 1935.

George W. McCandless, as Receiver of Duquesne Gas Corporation, Petitioner,
vs.
Maxime H. Furlaud, Carlos Reuter, Kingston Corporation, Byron Corporation and Chaucer Corporation, Respondents.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[November 11, 1935.]

Mr. Justice Roberts, dissenting.

I think that the decree of the Circuit Court of Appeals should be affirmed. I concur in the view that the promoters of Duquesne Gas Corporation took an unconscionable profit which they reaped at the expense of a credulous and avid purchasing public. This fact, however much it may invite animadversion, ought not to induce the courts to disregard settled principles in an effort to deprive the respondents of the fruits of their scheme.

An examination of the pleadings and the facts found leads me to the conclusion that the receiver of the corporation is without standing to recover from the promoters.

The bill recites in somewhat different sequence the facts which are set out in the opinion of the court. It does not state that the properties were not worth the amount in bonds, stocks, and cash which the Duquesne corporation paid for them. It fails to allege any fraudulent misrepresentation on the part of the respondents to purchasers of bonds or stock of the corporation. The allegation is made that Furlaud & Company, Inc. was, in the sale of the securities, a house of issue, meaning, of course, that it purchased the securities and resold them for its own account. Although the facts pleaded demonstrate that for some time after the organization of the Duquesne Corporation, and the issuance of its bonds and stock Furlaud & Company, Inc., by itself and its subsidiaries, was the owner of every share of stock and every bond issued and out-

standing, the bill asseverates, first, that the profit obtained on the sales of securities was a secret profit for which Furlaud and associates are accountable to the receiver and, secondly, that they stood in a fiduciary relation to Duquesne and "caused all the proceeds of the sale of the bonds and notes in excess of $2,937,989, plus legitimate expenses, to be diverted from the Duquesne Corporation for whose use and benefit the proceeds of the sale of said bonds and notes were intended and defendants Furlaud and Reuter fraudulently misappropriated said moneys to their own use." The last assertion is the nearest approach to an allegation of agency or trust for or on behalf of the corporation. The prayer is for an accounting by the defendants of the moneys received by them, apparently on the theory that such moneys were received as agents for the corporation. On its face the pleading is self-contradictory. If what the defendants took constituted promoters' profits the bill discloses that these were not secret profits taken to the disadvantage of innocent stockholders who had been brought into the corporation. Furlaud & Company and the other defendants were on both sides of the transaction and cannot be said to have deceived themselves as stockholders and bondholders and, upon familiar principles, those who took title to stock or bonds through them cannot assert rights higher than theirs. If, on the other hand, Furlaud & Company was a house of issue, dealing on its own account, it cannot have been an agent of Duquesne for the sale of bonds and stock.

The District Court denied a motion to make the pleading more specific and certain and the cause went to trial on the bill and answers. The proofs disclosed in detail the mechanics of the transaction whereby the promoters, at an expenditure of something in excess of $3,000,000, acquired $4,000,000 par value of first mortgage bonds, $1,000,000 of secured notes, and 675,000 shares of no-par common stock. Evidence was offered to prove that, at the date of the transfer, the property acquired was worth not to exceed $2,700,000. The defendants objected to this evidence on the ground that it was unsupported by any allegation in the bill. The court, nevertheless, received the proof and relied upon it for certain conclusions. There was also evidence that in the bond circulars issued by the defendants as a house of issue, and by a syndicate of bankers formed by the defendants to sell the securities

to the public, these statements were made: that the properties had been appraised at something over $7,000,000 and that the bonds and notes were issued by the corporation "in connection with the acquisition of properties and to provide cash for developments, extensions and other corporate purposes." The proofs conclusively show, and it is not disputed, that Furlaud & Company, upon its individual credit and that of its subsidiary, the Kingston Corporation, obtained the funds with which to make settlement for the bonds, notes, and stock with the Duquesne Corporation and reimbursed themselves for these loans out of moneys paid by brokers in the purchase of the securities.

It is quite true that Furlaud & Company, Inc. had, prior to receipt of the bonds, notes and stock, arranged for the sale of the bulk of the bonds to brokerage houses when, if, and as issued. This, however, is not an uncommon method of dealing and in itself is insignificant so far as the fairness or unfairness of the transaction goes.

In its final analysis the situation comes, as the District Court indicated, to this: that Furlaud & Company, Inc. advanced the purchase money for the gas properties, contributed $364,700 to Duquesne as working capital and in return received the securities. The court added that if without the circuity here resorted to Furlaud & Company, Inc. had thus bought the securities direct at an inordinately low price they could have done with them as they pleased. It held that they could not do with them as they pleased because of the method of settlement with the corporation to which they resorted. There is no specific finding by the District Court of fraud or misrepresentation on the part of Furlaud & Company, Inc., in the sale of the bonds. What is said is that the circulars misrepresented the facts. There is no finding that any present bondholder relied on any misrepresentation. Although it is insisted that Duquesne was insolvent from the moment of the settlement with Furlaud & Company, Inc. there is no finding to that effect. The District Court held that the promoters stood in a fiduciary relation to the corporation. It made no finding that the purchasers of bonds and notes were induced to purchase by misrepresentation; made no finding of loss or damage to such purchasers; made no finding that the purchasers understood Furlaud & Company, Inc. were acting as agents for Duquesne in the sale

of its securities but reached the conclusion, without any evidence to support it, that those who purchased bonds and notes from the promoters understood that the money which they paid in the purchase of the securities was to go *in solido* into the treasury of Duquesne. A moment's reflection will show that this could not have been the case. The very circulars which were issued, and on which the bonds were sold, showed that they were not being sold for par and that commissions were being paid for their sale. It is quite evident from the circulars that these commissions were not being paid by Duquesne but by the brokers who were selling the bonds as principals.

Upon principle, and upon authority, the corporation had no cause of action in the circumstances against the promoters and the receiver's rights could rise no higher.

First. The District Court held, and the Circuit Court of Appeals concurred, that the promoters were not answerable in respect of the no par value common stock issued to them and thereafter sold by them. This Court reverses the holding and makes them liable to account for all they received for the stock. This is in the teeth of *Old Dominion Copper Company* v. *Lewisohn*, 210 U. S. 206. There, as here, stock was issued for property. The claim was that the property was worth vastly less than the par of the stock issued for it. Additional shares were later subscribed for by the public. This Court, in a unanimous opinion, speaking by Mr. Justice Holmes, held that any wrong which had been done to the innocent subscribers could not be redressed in an action by the corporation. Here we have a much stronger case, for all the stock was subscribed for and taken by the promoters. There were no innocent subscribers. In such a situation the courts with practical unanimity hold that the corporation has no right of action.[1]

Second. On its face the transaction under investigation amounted to this and nothing more: The promoters paid themselves an exorbitant price in bonds, notes, stock, and cash for property which they turned over to the corporation they had promoted. The bonds and notes thus acquired they sold in the open market and as principals. If in such sale they misrepresented the value of the security they are liable to those whom they deceived. This

[1]See the authorities collected in the annotation to *Hays* v. *Georgian, Inc.*, 230 Mass. 10, 82 L. R. A. 1263-1265.

is not denied. It was stated at the bar that numerous actions had been brought against them on this basis. Although purporting to be purchasers of securities and sellers of the same in turn for their own account, they are now converted into trustees for the corporation which corporation they were in essence at the time of the transaction and which corporation had, therefore, full and complete knowledge of every factor in the transaction. This again is in the teeth of *Old Dominion Copper Company* v. *Lewisohn, supra.*

In support of its holding the court cites *Dickerman* v. *Northern Trust Company,* 176 U. S. 181; *Brewster* v. *Hatch,* 122 N. Y. 349; *Erlanger* v. *New Sombrero Phosphate Co.,* 3 App. Cas. 1218; *Gluckstein* v. *Barnes* [1900] A. C. 240; and *Yeiser* v. *United States Board & Paper Co.,* 107 Fed. 340. An examination of the opinion in the *Old Dominion Copper Company* case will show that it was there said the relevant observations in the *Dickerman* case were *obiter* and could not control the case in hand; that the *New Sombrero Phosphate* case and the *Gluckstein* case were distinguishable, as was the *Yeiser* case, the latter on the ground that the transaction was carried through after innocent subscribers had paid for stock; and that *Blum* v. *Whitney,* 185 N. Y. 232, (a later case than the New York case relied upon by the majority) was properly cited in support of this court's decision. The facts just stated clearly indicate that the decision now made in effect overrules the *Old Dominion* case. The so called fiduciary relation of promoters may be availed of by the corporation only in virtue of the equity of innocent stockholders defrauded by the promoters' scheme. So holds the *Old Dominion* case, and so hold many authorities which are in accord. It is said that the right of the corporation to pursue the promoters depends upon the circumstances under which the stockholders gave their consent to the transaction involved in the promoters' scheme. Nothing is disclosed in the opinion of the court to differentiate this case from the *Old Dominion* case save that, as asserted, but not found below, the transaction caused insolvency to the Duquesne Corporation and the suit is here brought by a receiver.

Third. It is of course true that a receiver represents creditors and stockholders; but the proposition is true only in the sense that what he recovers as assets of his corporation is dedicated first to the payment of creditors and afterwards to the liquidation of

outstanding shares. It has never been doubted that his right of action for a fraud committed upon the corporation by a third person is no greater than and no different from that available to the corporation. It is a novel doctrine that, if individual creditors have at the date of the receivership their own causes of action against third parties for fraud or misrepresentation, upon the appointment of a receiver these causes of action are assigned, in law to the receiver. We know of no authority for such a proposition and none is cited in the opinion of the court. Courts which have considered the question have decided against the right of a receiver to maintain a suit such as this one.[2]

The opinion goes further, and holds not only that these individual causes of action may be grouped in the receiver, but that he as assignee is not subject to the rules as to allegation and proof by which the bondholder would be bound in an action for fraud, misrepresentation or deceit. This is to confuse separate causes of action fundamentally differing both in their substance and in their incidents. Any amount recovered by the receiver in this action will go into the corporate treasury and be distributed therefrom to the creditors of the corporation. It appears from the record that the bondholders have brought a foreclosure suit upon their mortgage. They will in that action first avail themselves of the security pledged under the mortgage. They will become general creditors as to any amount by which their security is deficient. The record does not inform us how many such general creditors,—sellers of merchandise, lenders on unsecured paper, or employees and the like,—there are. Certainly these have no equity and no vestige of claim against the promoters arising out of the promotion of the Duquesne Corporation. And yet a recovery here will inure to their benefit as well as to that of the bondholders. If, as is said, the receiver represents the bondholders, shall the obtaining of a decree in this action operate as *res judicata* in the other actions brought by bondholders and now pending? The opinion does not answer the question. It seems clear that a suit by the receiver must be in the right of the corporation, and that the most he can claim is what the corporation could claim, namely, a derivative right of suit based upon fraud perpetrated upon innocent shareholders who were such at the time of the consummation of the

[2] *Tompkins* v. *Sperry*, 96 Md. 560; *Bostwick* v. *Young*, 118 App. Div. 490, 496, affirmed 194 N. Y. 516; *Young* v. *Stevenson*, 180 Ill. 608.

scheme. Upon the facts pleaded and proved there can be no such derivative right in this case.

Fourth. We are told that the action may be maintained by the petitioner in virtue of the fact that the transaction was forbidden by a provision of the Constitution of Pennsylvania, and a statute passed to implement it, voiding all fictitious increases of capital stock or indebtedness of corporations and forbidding the issuance of stocks or bonds except for work and labor done or money or property actually received. The point was apparently not made or considered below. It cannot avail the petitioner.

The constitutional provision is not self-executing.[3] There is nothing in the law of Pennsylvania justifying a suit by a receiver in circumstances such as here disclosed to recover for the corporation alleged illicit profits; and the Supreme Court of the Commonwealth has clearly indicated that such a bill will not lie by the corporation to recover for promoters' profits or alleged fraud in issuing stock at an overvaluation for property where, as here, all the stockholders approved the transaction.[4]

As we have above pointed out, the receiver's rights can in no way differ from those of the corporation. This Court ought not to create a trusteeship upon an assumption of a State policy which is not recognized by the courts of the State.

The decree of the Circuit Court of Appeals should be affirmed.

Mr. Justice McReynolds, Mr. Justice Sutherland and Mr. Justice Butler concur in this opinion.

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[3] *Yetter* v. *Delaware Valley Railroad*, 206 Pa. 485; *Grange National Bank* v. *Collman*, 306 Pa. 200.

[4] *Spangler Brewing Co.* v. *McHenry*, 242 Pa. 522, 529. See also *Wood* v. *Corry Water-Works Co.*, 44 Fed. 146 (*U. S. C. C. W. D. Pa.*). In contrast, see *McElhenny's Appeal*, 61 Pa. 188; *Densmore Oil Co.* v. *Densmore*, 64 Pa. 43; *Bailey* v. *Pitts &c. Co.*, 69 Pa. 334, where there were innocent subscribers for shares, who were ignorant of the profits taken by the promoters.